

CHAPTER - I

1. INTRODUCTION

1.1 General Background

Income tax is introduced first in Great Britain in 1799 in order to the Finance War with the France. Such, a tax was adopted as a substituted for custom and exercise duties in rising revenue. It was treated as a temporary ax until 1860. Therefore, it was made a permanent tax. Federal income tax was first introduced in USA in 1862. So into finance the expenditure of the civil war it assumes significance in 1913 after the 16th amended to US contribution. The other company, which flows suit, were Italy in 1864, Australia in 1915, New Zealand in 1891 and Canada in 1917. Income tax was developed as an important source of government revenue in many other countries. After the First World War, income tax developed somewhat slowly with many ups and down. The increasing revenue requirement, especially during the war and nation civil and rising requirement of his fiscal power of government contribution force to income tax activities. In the beginning, income tax lies in UK and New Zealand in 1909. The progressive method was first used in case of super tax.

In content of Nepal authentic records regarding taxation in Nepal were not available in ancient and Medieval period in ancient Nepal, the small rules used to levies charge on the layers and merchants though land revenue was the principal source of income in ancient Nepal. There did prevail irrigation tax and religious memorial conversion tax in times of King Amsuverma of Nepal.

An ancient Nepal, taxes were levies in the form of both cash and kind. A certain portions of agricultural products was payable to the King in the form of tax. Taxes were paid in gold. Compulsory handwork by artists and labor fee of cost to King was also a common method of paying tax the type of taxation was very seasonal (temporary) and taxes were collected for a particular purpose.

The principal source of income tax in Nepal during 1768-1846 were land and homestead tax, monopolies customs, transit and market duties mines and mints and export of forest products, birds, animals, and fines. The chief purpose of the tax policies during this period was the maximization of income. Local people pay voluntary taxes were normally collected at three ways;

- a) Royal Place Level
- b) Government Place Level
- c) Local Level

The job of the collecting customs transit and market duties and excise duties was given on contract. Taxes were levied in some parts of Teri at certain rates or ornaments, textiles, falcons, horse, elephants, home etc. Income from forest related mainly in the form of duties on timber exports.

During this period various tax imposed were reduced at the base level and were levied briefly on occupations and economic activities not on income or property. The methods of direct taxation were very much restricted to land tax and specific levies like Darshanbhet, Salami, Walk and etc. There was no tax.

During the period of 1846-1905 of the aristocracy rule of Rana Family. The imposition and collection of taxes were governed and regulated by the Royal Family only those taxes, which fitted with the aims. Necessities and ideas of the rules of Prime Minister were levied. The accounts of income and expenditures of the state were not made public, no budget was ever formulated during the Rana Regime infact, and there was no difference between the revenue on the country and that of the Prime Minister. The principal source of income in Nepal till 1951 were land revenue, custom and excise tax in sort of lump sum contracts, royalties on falling of trees, royalties of supply of porters and soldiers, entertainment tax and a few other minor taxes. There was no direct tax in the state except land revenue if it was not collected on contractual basis and salami which the government servants used to pay out of their salamis at a nominal rate. The salami was however, abandoned in 1951. Since a major portion of the revenue in Rana period used to accrue from the seasonal

contracts, the necessity was not felt for the development of effective revenue administration system.

After the down of democracy, the idea of introducing income tax in Nepal originated along with the first budget on 21st Magh 2008. Then Finance Minister in first budget speech said 'A Proposal to Levy an Income Tax Including Tax on Agriculture Income is under Consideration.' After that, so many reforms in tax of laws in Nepal and several attempts were made to introduce income tax in subsequent years. Different types of tax law were introduced and abolished. However, it could not introduce successfully done. However, it was actually introduced only in 2017 when Finance Act 2016, Income Tax Act, 2017 was enacted. At the beginning, equivalent tax, rates with progression and exemption limit were prescribed by the Finance Act of 2017 and afterwards to all companies, private firms, individuals and families. The marginal rate of taxation prescribed by these acts was 25 percent. Since income tax was imposed only on income from business profit and remuneration tax could not cover all the source of income and so was replaced by the Income Tax Act 2019 in 2019. Income Tax Act 2019 with 29 sections divided the heads of incomes into 9 parts covering business, professions and occupations, remuneration, house and land rent, cash or kind investment, agriculture, insurance business, agency business and other sources; the act was amended in 2029 extensively. However, considering this act incapable of fulfilling the needs of the times, it was replaced in 2031 by another act.

As already stated Income Tax Act, 2031 replaced Income Tax Act 2019. This act having 66 sections, and classified the sources of income into 5 heading namely; Agriculture, Industry & Business, Professions or Vocation & Remuneration, House and Land Rent, Other Sources.

The act had introduced the chargeable income and admissible expenses of each head of income. The other feature of this act was provision of expense and others. This act is not sufficient in next time the amended in 2031 has made advanced than the former income tax acts. However, it had several weaknesses

and used many vague or unclear words like reasonable appropriateness etc. Income Tax Act 2031 was revised for 8 times. It has also provided high discretionary power to the tax officer in the matter of tax assessment. Similarly, it did not succeed to cover the large portion of income under different cases.

In the courses of development and modernization of income tax system, the new "Income Tax 2058" has been enacted. Similarly, the new "Income Tax Rules 2059" have also been enacted for effective implementation of the objectives of this act. The new act has introduced and classified the effective from 2059-02-27. This act has classified the heads of incomes into three categories via, employment, business and investment. The new income tax act has 143 sections. This act was brought in Nepal to avoid the following defects of Income Tax Act 2031; Narrow base of tax, taxing only the income originated in Nepal, Dispersion of tax related acts i.e. income tax related provisions were given different acts, Low penalty rate to tax evader Incompatible to self- assessment system and Unsuitable to modern economy.

In the modern income tax of Nepal were collected in various forms in ancient era. The history of modern Income Tax is not very old in Nepal. The idea of introducing Income Tax in Nepal originated in the early 1950s, when a multiparty democracy political system was introduced in 1951 then the Finance Minister in his budget speech declared the intention the government levy and Income Tax. Nepalese Income Tax is amended for eight times for the period of 28 year. Government of Nepal framed Income Tax Rules 2059 in 2059 to help clarifying the acts.

Income Tax was imposed in Nepal by the First Parliamentary Government in 1959. Income Tax Act 1962 was enacted in 1962 replacing business, Profit and Remuneration Tax Act of 1959. The Income Tax Act, 1962 was replaced by Income Tax Act, 1974, which was amended for eight times and existed for a period of 28 years. The Income Tax Act, 1974 and all the Income Tax related provisions made under other special enactment have been repealed and the existing Income Tax Act, 2058 became effective since Chaitra 19th, 2058 (01,

April 2002) to make implementation system effective GON of Nepal framed the Income Tax Rule 2059.. The Act governs all Income Tax matters and is applicable throughout the Kingdom of Nepal. It is also applicable to residents residing wherever outside Nepal.

1.2 Focus of Study

The focus of the study is how to collect and mobilize the internal resource. The selection of tax base is an important constituent of corporate tax structure. The different tax base are gross assets business expenditure, value added tax, cash flow and book profit each of which has its own merits and demerits. Most of the countries prefer book profit as the tax base as it is stronger and superior base than other tax base. The profit usually includes trading profit and computed by taking revenue and subtracting such expenses, which are incurred in generating this revenue. The corporate tax rate of Nepal has undergone a substantial change over the year tax rate structure was different in case of companies including government companies and public limited companies in the private sector. The government of Nepal has thus rationalized the corporate tax structure so much, so that it is now comparable with many other countries.

In order to the requirements for day-to-day administration and development government collects resources through various sources, principal among which them being the government revenue collect through the both tax and non tax source. But low rate of growth of economy, low level of income as well as the rate of saving and inefficient tax administrator make the collection of tax revenue a different task in Nepal besides, high tax payer often adversely affects the private enterprise and initiatives and contributes to decline net investment capacity. As a result, the proportion of the government revenue in national income stands less. In this cause the study explores will try to corporate tax contribution on government revenue in Nepal.

1.3 Statement of the Problem

In developing country like Nepal, the objectives of income tax could be generating revenue in order to help or finance development activities and to help establish social justices through income distribution, considering these objectives, since the time Income Tax introduced in Nepal, several changes has been making in Tax Laws, Tax Act, Tax Policy, Tax System and Tax Procedure etc. The idea of introducing Income Tax in Nepal originated in the early's 1950. But, the first elected government of Multi- Party Democracy System is 1959, introduced Income Tax in Nepal, at that time Income Tax was levied only on the business profit and salaries after three years experience of Income Tax in 1962 Income Tax was applied to income derive from different source. Since 1974, Income Tax sources have been re- enumerated into five sources however, agriculture income had been kept outside the tax rat except a few years through the financial plan.

The concern of every nation of the world is economic development; least developed countries are facing numerous problems in the process of economic development. Nepal is not an exception to this process of economic development. Nepal is not an exception to this condition about 42 percent of total population is below the poverty line. Due to various internal and external reasons, Fiscal Year 2002/2003 could not appear as a successful year from the perspective of peace, security and development

Lack of managerial efficiency is one of the major problems of Income Tax in Nepal. It is also a lack of effective personnel management, reward and punishment system, poor income tax assessment procedure, effective implementation of self-assessment of tax, poor tax information system, and education of taxpayers and very narrow coverage of income tax, tax evasion tax avoidance and proper utilization of tax planning. Corruption, quality of paying tax, ability to pay tax is another major problem of Income Tax in Nepal.

Similarly, most of the taxpayers are ordinary people or without having sufficient tax related knowledge nor the capacity to hire the tax experts, complexity of income tax law and tax assessment procedure, ill behaviors of tax administrators, under delay in tax assessment, lack of information are the major problems of these days that the tax payers of Nepal are facing these types of problems of tax paying habits of Nepalese people is very poor but tax evasion habit of such people is increasing day – to – day. It is due to lack of knowledge, zero incentives to regular tax payment, administrative harassment and poor enforcement of fines and penalties. Likewise, evasion of income tax, reason for wide spread evasion of income tax could be inefficient tax administrator wide spread practices of illegal business structure to maintain accounts, poor tax morality, tax payer's compliance in Nepal and supersede of law by the persons who are in the power and authority. In the developing country like Nepal, it is necessary to increase the government revenue. Government revenue is collecting the main source of tax and non tax. In the collection of government revenue there are apparently many problems there is no have to face due to lack of knowledge to pay the corporate tax payer. So the present study tries to solve the following problems.

-) Which sector contributes the maximum government revenue?
-) What is the major sector to collect the corporate tax?
-) How to do control the corporate tax avoid and erosion in corporate sector?

1.4 Objective of the Study

The main objective of the study is to effective tax collection and contribution to government revenue. Other specific objective is as follows;

-) To examine the status of corporate tax and to explore the tax collection in different corporate sector.
-) To explore the problems and challenges in corporate tax procedure.
-) To provide the package of suggestion to tax avoid and tax evasion in corporate sector.

1.5. Significance of the Study

In the developing country like Nepal, the implanting of Income Tax minimized because it is covered huge amount of Government Revenue. It requires higher amount of financial resources of development programmed. The resources collect internally are sufficient to run day-to-day administration of the country but the revenue surplus is not adequate to undertake the developmental activities. So, the country is heavily dependent on the foreign aids and grants to undertake its developmental activities. Corporate tax is one of the most important sources of collecting government revenue from Income Tax. Therefore, the corporate tax plays vital role in the government revenue of the country. It is a regular source of Income Tax too.

Thus, the study try to find out the problems and difficulties associate in the collection of corporate tax as a facilities and benefits provide by the Income Tax Act 2058 contribution of corporate tax on income tax total tax and direct tax revenue of Nepal. It has been also tried to suggest and recommends in some possible areas of reform in income tax with refers to corporate tax. There are many ideas on various tropics Income Tax but very few have study in detail on effectiveness of corporate tax in Nepal. So this thesis is direct towards acquiring information about Income Tax collection from corporate tax, which has not been studied in detail in this field. Thus, this study is useful to all the concern parties, for researchers, academician and others.

1.6. Limitation of the Study

All research study is to be done to solve particular research problems. It requires various kinds of data materials and other relevant information, which cannot sufficient to the researcher. This study cannot especially from the frame of limitation, this study mainly base on secondary data as well as primary data.

) This study is mainly based on published secondary data and information related to corporate tax as made available by NRB tax office and minister of finance from last five year published data.

-) The methodology is followed in this study is not designed by advanced and sophisticated technique.
-) Also non availability of plentiful literature on the subject has handicapped the study to some extent.
-) This study is only in corporate sector of Nepal.
-) Time and resources constraints may limit the area covered by study.

1.7 Organization of the Study

The research outlook has been divided into the following five chapters each devoted to some aspect of the study on effectiveness of corporate tax with reference to government revenue in Nepal. The chapter areas follow;

- a) Introduction
- b) Literature Review
- c) Research Methodology
- d) Presentation and analysis of Data
- e) Summary, Conclusion and Recommendation

CHAPTER - II

2. REVIEW OF LITERATURE

2.1 Conceptual / Theoretical Review

2.1.1. Revenue

Revenue is regular income of government from internal resources for execution of different bodies of nation. According to Revenue Leakage (Investigation and Control) Act 2052: "Revenue means the amount that is to be paid to government as custom duty, excise duty, income tax, entertainment tax, hotel tax, sales tax, vehicle tax, rent tax, contract tax, property tax and the word also indicates other taxes according to existing law." Revenue amount is collected through different medium from public people and spent from state for welfare of people, so it is also called public income. Government levies custom, excise, income tax, VAT, land tax, fees and penalties as source of revenue. Revenue can be divided into tax revenue and non tax revenue. Government income specified in act and law to be paid by person, firm, industry, business, trade, profession or organization for execution of some task or work or for holding of some kinds of assets is known as tax revenue. For example: custom, excise, land tax, VAT etc.

Revenue gained by government for distribution of public service or for public service or for direct facilities provided or for fees and penalties to state against violation of rules and regulation is known as non tax revenue. For example: income from sales of government goods and services, principle, interest, dividend, royalty, fine, penalty, seizing etc. are non tax revenue. Sources of revenue:

- a) Taxes
- b) Fees
- c) Amount for goods and services provided

- d) Fine/penalty
- e) Franchise cost
- f) Gifts and donations

2.1.2. Tax

Tax is an important source of revenue for government. It is compulsory provision to citizen imposed by law to pay as monetary term to government without any expectation of some specified return. Economists and scholar have expressed their view in tax as follows:

"A tax is a compulsory contribution imposed by a public authority irrespective of the exact amount of service rendered to the taxpayer in return and not imposed as penalty for any legal offence." -*Dalton*.

"A tax is a compulsory contribution of wealth of a person or body of persons for the service of public powers." – *Bastable*

"A tax is a compulsory payment to government without expectation of direct expenses of direct return in benefit to the taxpayer." – *P. E. Taylor*

"Taxes are compulsory contributions to public authorities to meet the general expenses of the government which have been incurred for the public good and without reference to special benefits." - *Findlays Shirras. (Lekhi, 2000:146)*

"Taxes are general contribution of wealth levied upon persons, natural or corporate to defray expenses incurred in conferring common benefit upon the residents of the states." – *Plehn (Dhakal, 1998:2)*

"Tax is a compulsory contribution from a person to the government to defray the expenses incurred in the common interests of all without reference to special benefits conferred." – *Professor Saligman (Lekhi, 2000:146)*

Among above, the first three states that the tax is compulsory levy and the taxpayer does not have any right to receive direct benefits from tax paid. The remaining definitions also clears about the expense of collected tax in common

interests of residents of nation. According to definition, tax has major three characteristics:

- a) It is a compulsory monetary contribution.
- b) Taxpayers should not expect special treatment as a return of tax.
- c) Amount collected from tax should be expended for public of whole nation.

Taxes are levied primarily to raise revenue for the government expenditures, although they raise other purposes as well. The concept of modern tax contains different fundamental principles such as:

- a) No taxation without representation. Tax can be levied only with the approval of citizens through their representatives.
- b) Foreigners are to pay more tax than citizens
- c) Progressive principle i.e. more tax for more income.
- d) Tax should be collected compulsorily.
- e) Taxpayers are compelled to pay as their liability.

Tax can be classified into direct and indirect tax.

i) Indirect tax

Indirect tax is imposed on one person but paid partly or wholly by another. It is transferable and people pay tax when they receive or consume goods or services. It is transferable and people don't feel burden of lump sum. There is mass participation because every person pays tax for receipt of goods or services. Indirect tax can be charged at higher rate for harmful goods such as cigarette and alcohol to discourage them. So indirect tax is flexible. Examples of indirect taxes are customs, excise, value added tax, entertainment tax etc.

There are some limitations of indirect tax. Every person either rich or poor has to pay equal amount of tax for reception of goods or services so it is tougher for poor. The higher rate, if imposed, may reduce consumption and it effects on production and employment. There is no certainty about collection of indirect tax.

ii) Direct tax

Direct tax is paid by same person who is legally imposed. It is paid according to the income or property earned by a person. It is found equal with property. There is certainty about time, design and process of payment. Taxpayers can easily estimate their liability and government can easily increase or reduce according to needs. Income tax, contract tax, vehicle tax are examples of direct tax. Direct tax is levied on direct persons, so they may not be ready to pay voluntarily. And of course they try to pay lowest tax as possible as and also exercise for tax evasion. Direct tax is also expensive for collection. Direct tax discourages private saving and investment and there is lack of mass participation.

2.1.3. Income

Income generally means monetary or equivalent gains during a period from property, business, labor etc. According to Dictionary of Economic Terms, income mean " The wealth measured in money, which is at the disposal of an individual or a community per year or other unit of time; it may be regarded as a flow of purchasing power which may be expended at once on goods or services or retained for the purposes of capital accumulation."

According to Professor Haig " Income is net accretion of economic power between two points in time and this net accretion of economic power consists of two distinct parts: consumption and net capital accumulation."

Henry Simons has more clearly defined the term income by algebraic method. According to him, income is algebraic sum of two items:

- i) The person's consumption during the period, and
- ii) The net increase in the individual's personal wealth during the period.

Symbolically,

$$Y = C+W$$

Where,

Y = Income

C = Consumption

W = Change in wealth (Due & Lander, 1977: 223)

There is difficult to find specific definition of income all over the world specially, for the purpose of tax. For example Sec 2 of Indian tax act 1961 keeps profits and gains, dividend, voluntary contributions received by charitable trusts, value of any perquisites or profit on lieu of salary, any capital gain, winning from lotteries, cross word puzzles etc under the head of income. *(Krishna Swami, 2006: 18)*

Income Tax Act 2002, Nepal describes three major heads of income, income from employment, income from business and income from investment. Section 5 describes that taxable income of a person for an income year is equal to the amount as calculated by subtraction of reduction from the total of total assessable income of person from each of the income head of employment, business and investment.

2.1.4. Income Tax

Income tax as the word refers itself as tax on income. In a broad sense, income tax is a levy based upon the productions or receipts or gains of the taxpayers within a definite period of time. *(Encyclopedia America, vol.14:749.)*

There is no specific definition for income tax as it varies for countries according to diversity of economic structure, nature of government and the status of people. In General income tax is imposed on net income. Net income comes after subtraction of the cost of production from gross income. In practice the expenses incurred in earning the income and appropriate exemptions are deducted to find out the taxable income. Net income may be real income or money income. Real income is more comprehensive and includes not only money income but also other incidental advantages. Real income should therefore be the true index of ability to pay. So income tax should be charged

on real net income of the individual and not on his net money income.
(Agrawal, 1967:104)

There are two types of income tax such as

- i) Personal income tax: Levied on the personal contribution rather than an extraction of economy. Here assumption is that all income is directly received by an individual.
- ii) Corporate income tax: Tax is assessed on the profit of the corporation. It is considered the best one because the bulk of business activity in most advanced countries is carried on under the corporate form of organization.

2.1.5 Corporate Tax

In the content of Nepal, the term business includes an industry, a trade, a profession, a vocation, an office and an isolated transaction with a business character of a past, present or prospective business and the conduct of electronic commerce. The law has clarified that business does not include employment. A company is a corporate body incorporated as per the law. It is an artificial person which can sue. In Nepal, company is regulated under Company Act 2053. But this act has not given the specific definition of company. It only specifies that there is need of 7 promoting members if it is a public limited company. Income Tax Act, 2058 has also defined a company for the purpose of tax assessment. According to section two (1) of the Act, a company means any corporate body or unincorporated association, committee, institution, society or group of persons or a proprietorship firm whether or not registered or a trust. According to law the word company also includes a firm registered under Partnership Act 1964 or not registered having 20 or more partners a retirement fund, a co-operative, a unit trust of a joint venture, a

foreign company and any foreign institution specified by Director General as Company.

Corporate law is about big business, which has separate legal personality, with limited liability for its shareholders, who buy and sell their stocks depending on the performance of the board of directors. Corporate law is the law of the most dominant kind of business enterprise in the modern world. Corporate law is the study of how shareholders, directors, employees, creditors, and other stakeholders such as consumers, the community and the environment interact with one another under the internal rules of the firm. Corporate law is a part of a broader company's law. Other types of business associations can include partnerships or trusts or companies limited by guarantee. There are some characteristics of corporate tax. *(Kotrappa, G.1996)*

-) Separate legal personality of the corporation.
-) Limited liability of the shareholders.
-) Transferable shares.
-) Delegated management, in other words, control of the company placed in the hands of a board of directors.
-) Investor ownership,

The last of these defining features is contested. For a start, it pointed out that shareholders, do not own corporations, they own their shares. Ownership of a corporation is complicated by increasing social and economic interdependence, as different stakeholders compete to have a say in corporate affairs. In most developed countries company boards have representatives of both shareholders and employees to "codetermine" company strategy. Corporate law is often divided into corporate governance which concerns the various power relations within a corporation and corporate finance which concerns the rules on how capital is used. *(Kotrappa, G, 1996)*

2.1.6. Company and Types of business entity

The word "corporation" is generally synonymous with large publicly owned companies. In the United States, a company may or may not be a separate legal entity, and is often used synonymously with "firm" or "business." A corporation may accurately be called a company; however, a company should not necessarily be called a corporation, which has distinct characteristics. A company means "a corporation — or, less commonly, an association, partnership or union — that carries on industrial enterprise." (*Black's Law Dictionary*)

The defining feature of a corporation is its legal independence from the people who create it. If a corporation fails, shareholders will lose their money, and employees will lose their jobs, but neither will be liable for debts that remain owing to the corporation's creditors. This rule is called limited liability, and it is why corporations end with "Ltd."

However, despite this, corporations are recognized by the law to have rights and responsibilities like actual people. Corporations can exercise human rights against real individuals and the state and they may be responsible for human rights violations. Corporations can even be convicted of criminal offences, such as fraud and manslaughter. (*Company Act*)

Corporate governance is primarily the study of the power relations between the board of directors and those who elect shareholders in the "general meeting" and employees. It also concerns other stakeholders, such as creditors, consumers, the environment and the community at large. One of the main differences between different countries in the internal form of companies is between a two-tier and a one tier board.

Recent literature, especially from the United States, has begun to discuss corporate governance in the terms of management science. While post-war discourse centered on how to achieve effective "corporate democracy" for shareholders or other stakeholders, many scholars have shifted to discussing the law in terms of principal-agent problems. On this view, the basic issue of

corporate law is that when a "principal" party delegates his property (usually the shareholder's capital, but also the employee's labour) into the control of an "agent" there is the possibility that the agent will act in his own interests, be "opportunistic", rather than fulfill the wishes of the principle. Reducing the risks of this opportunism, or the "agency cost", is said to be central to the goal of corporate law. (www.wikipedia.com)

2.1.7 Classification of Business

There are two types of business one is Limited Liability and another is Unlimited Liability.

A) Limited Liability: Limited Liability means to be bounded by legal responsibility for obligation especially cost or damages. In this sense owners are liable for a company's debts only up to the value of their shareholding. Categories of companies vary from country to country and go by different names. The main difference between public and private company is public company can sell their shares to the general public. In general private company tends to be smaller than public companies. However, some of Nepalese biggest companies are privately owned. Thus, in the limited liability organization shareholder investors are limited up to their share or investment amount.

The limited liability organization can be divided into two categories Limited Company and Corporation

1) Limited Company: Limited Company with the limited liability. So a limited liability business organization is a type of began entity. It is similar to a corporate and a limited liability partnership. It has some advantages over sole proprietorship and unlimited partnership. The limited liability organization

again can be divided into two categories Private Limited Company and Public Limited Company.

a) Private Limited Company: Private Company means a company incorporated under this act, which limits the number of its shareholders to fifty, is prohibited from issuing public invitations to subscribe to its shares and debentures, and is subject to restrictions on the sale or mortgage of its shares or debentures to persons other than shareholders without the approval of the Board of Directors.

b) Public Limited Company: Public Company means a company other than a private company. Shareholders of Public Limited Company is more than private limited company or above fifty persons. It is subject to sale or mortgage of its shares or debentures to persons other than shareholders.

2) Corporations: Corporation is a legal entity. According to Oxford English Dictionary term "Corporation" is derived from Latin words Corpus (body), representing a "Body of People," i.e. a group of people authorized to act as individuals. The term university also used to refer to a group of people but now refers specifically to group of scholars. However in colloquial usage "corporation" usually refer to commercial entity set up in accordance with a governmental framework. In Nepal there exist two types of corporation fully owned and semi owned by the government. For instance Nepal Airlines Corporation, Nepal Telecommunication Corporation, Timber Corporation are example of fully government owned organizations. Similarly, National Industry Development Corporation, Salt Trading Corporation, National Insurance Corporation are examples of semi government owned corporation. Most of these corporations are established under Panchayat regime by special character.

The defining feature of a corporation is its legal independence from the people who create it. If a corporation fails shareholders will lose their money and employees will lose their jobs, but neither will be liable for debts that remain owing to the corporation's creditors. This rule is called limited liability and it is

why corporations end with "Ltd." In the words of British judge, Walton J, a company is "only a juristic figment of the imagination lacking both a body to be kicked and a soul to be damned."

However despite this, corporations are recognized by the law to have rights and responsibilities like actual people. Corporation can exercise human rights against real individuals and the state and they may be responsible for human rights violations. Just as they are "born" into existence through its members obtaining a certificate of incorporation, they can "die" when they lose money into insolvency. Corporations can even be convicted of criminal offences such as fraud and manslaughter.

Corporate governance is primarily the study of power relations between the board of directors and those who elect shareholders in the "general meeting" and employees. It also concerns other stakeholders such as creditors, consumers, the environment and the community at large. One of the main differences between different countries in the internal form of companies is between a two tier and one tier board.

B) Unlimited Liability: Unlimited Liability means to unbounded by legal responsibility for obligation, especially lost or damages. Thus, in the unlimited liability organizations are the investor proprietor or partners are unlimited up to their share or investment amount.

1) Sole Proprietorship: Sole Proprietorship is the oldest, most common and simplest form of business organization owned and managed by one person. It can be organized very informally, is not subject to much state regulation and is relatively simple manage and control.

2) Partnership: Partnership is an association of two or more persons to carry on as co-owners a business for profit. In other words, if two or more individuals do nothing more than verbally agree to conduct business as owners, a partnership is formed. The partnership consists of relationship between two or more persons embodied in an agreement. Certain of the agreement establish

rights and duties between the partners and regulate their conduct as they transact business.

A source of Partnership Law has been confided in Partnership Act 1964 (2020). According to the act no saturate filling of association and the articles of association needs to form and operate a partnership business. However it needs a partnership deed that assist individuals in creating and defining the relationship between partners. It can be useful reference when the partnership agreement is select on a particular topic.

2.2.1.8 Special Provision of Entities

In the Income Tax Act 2058 has presented special provision for entities. It includes principles of taxing entity, taxing distribution boy entity etc. Here, it should be noted that entity means an organization established under the law whether profitable or non- profitable. For the purpose of Income Tax Act 2058, it includes a partnership, trust or company, or village development committee, district development committee, metropolitan city, sub metropolitan city, municipality or a government or a political subdivision of a government. It also includes a public international organization established under treaty and a permanent establishment of an individual or an entity that is not situated in the country in which the individual or entity is resident.

The following principles are laid down by Income Tax Act 2058 for the taxation of entity (section 53)

-) An entity is liable to pay tax separately from its beneficiaries.
-) Distributions of entities, i.e. dividends may be taxed to beneficiaries in the final withholdings.
-) Amounts derived and costs incurred by an entity are treated as derived or incurred by the entity and not by any other person.

-) Assets owned and liabilities owned by an entity are treated as owned or owed by the entity and not by any other person.
-) Foreign income tax paid in respect to the income of an entity, whether paid by manager, beneficiary or the entity, is paid by the entity.

Transactions between an entity and its managers and beneficiaries are recognized. (*Puspa Raj Kandel, pp 19*)

2.1.9. Tax Rate of Entities

There are different rates of taxes applicable to different types of entities. For example;

-) The taxable income of an entity for an income year is taxed at the rate of 25 percent.
-) The taxable income of a petroleum industry or bank or other financial institution for an income year is taxed at the rate of 30 percent
-) Industrial enterprise which is engaged in an industrial activity related to a special industry or which is related to an infrastructure project like road, bridge, tunnel, ropeway, or flying bridge constructed by the entity or any trolley bus, or tram manufactured by the entity is taxed at the rate of 20%. Accordingly, the taxable income of an entity wholly engaged in power generation, transmission, or distribution for an income year is taxed at the rate of 20%. Note that special industry means and industry of a type according to section 3 of the industrial enterprises act 1992 other than an industry producing.
 - i) Cigarettes, Bidi Cigar, Chewing Tobacco, Khaini or other goods of a similar nature using tobacco as the basic raw material.
 - ii) Alcohol, beer or other goods of a similar nature.

2.1.10. Corporate Tax Rate

No changes in the existing tax rate payable by domestic companies for the fiscal year 2008/09. In the Income Tax Act 2058 there are following tax rate is given

) Banks and financial institutions	30
) General Insurance Business	30
) Cigarettes, Bidi Cigar, Chewing Tobacco Khaini, Liquor, Beer	30
) Petroleum companies	30
) Special industries	20
) Export industries	20
) Power generation, transmission, distribution, infrastructure projects etc	20
) Other entities not covered above	25

Additional tax of 1.5% has been abolished with effect from this Financial Year.

) Additional tax of 1.5 percent has been abolished by Finance Bill for 2008/09.

) House rent tax shall be levied at the rental income at the rate of 10 percent against existing rate of 15%.

) Tax at the rate of 5% shall be charged on the dividend paid by the resident entity to resident or non-resident person. Unlike in previous year 10% tax on dividend paid to non-resident person has been abolished.

) The existing TDS of 1.5% on the premium paid to resident insurance companies has been abolished from this Fiscal year. However, TDS @ 1.5% is continued to be levied on premium paid to non-resident insurance companies

) TDS on contract amount paid to Non-resident person by resident person:

) In case of service contract @10%

) In other cases - @ 5% (Income Tax Act 2058)

2.1.11. Tax Evasion

Tax evasion is the way of reducing tax liability by illegal means. It is done through different ways like none reporting of income making fraudulent changes in account books, maintaining multiple sets of accounts, operating business transactions under different names, opening bank account in dummy name, over reporting of expanses, fragmentation of income, transfer pricing

etc. Tax evasion is unethical, illegal and uneconomic activity. It is unethical because the activity of not paying tax is against moral ethics. It is illegal because the law does not permit to evasion the tax. In the same way, it is uneconomic because it promotes black money, i.e. underground economy in a country. Such types of activities do no promote healthy economic in a country. *(Puspa Raj Kandel; 2003)*

2.1.12. Reason for Tax Evasion

Basically the reason of tax evasion can be divided into two non tax factor and tax factors. Non- tax factors include educational background, price policies and the government, government rules and regulations, public sector salaries, government's expenditure policy and others. Tax factors include tax rate, tax base, tax structure, penalty system, probability of detection, magnitude of the strictness of penalty and possibility of detection, magnitude of the mainly, tax factors are more concerned with the tax evasion on income from legal activities, weather non-tax factors are related with illegal activities. *(Puspa Raj Kandel; 2003)*

2.1.13 Types of Tax Evasion

There are three types of effects of tax evasion in the economy. They are loss of revenue to the state. Redistribution of income which affects the efficiency of resource allocation in the economy and creating wrong statistics leading to errors in government policies. Evasion of income tax is also associated with the evasion of sales tax, excise duty, custom duty and so on. Since the government imposes higher tax rate to fulfill the growing need of the revenue, it is the honest taxpayers that really bear the burden of tax. *(Puspa Raj Kandel; 2003)*

2.1.14 Problems of Tax Evasion

Tax evasion is a major problem to the government in developing countries. There are several types of tax evasion.

- a) Unilateral (taxpayer himself)

- b) Bilateral (with the connivance or assistance of government official)
- c) Trilateral (from the collusion of tax officers, tax auditors and tax payers)
- d) Multilateral (all parties from government to tax payer)

In a world of tax evasion, it is very difficult to choose between businessmen, professional, a person in service or a politician who is not a tax evader. It we tear the mask the face looks alike (*Puspa Raj Kandel; 2003*)

2.1.16 Tax Avoidance

Tax avoidance is saving taxes without actually breaking the law. It is using the loopholes of the tax law. It is not illegal but unethical. According to GSA Wheat craft says, " Tax avoidance is the art of dodging tax without actually breaking the law." In the other words, it is a transaction entered into with full legal backing. However, such activities are of those kinds that the legislature does not want to encourage. The following are the criteria used by English and Indian court to find out tax avoidance. (*Puspa Raj Kandel; 2003*)

-) Use of colorable devices,
-) Defeating the genuine spirit of law,
-) Twisting of facts,
-) Taking only strict sprit of law and suppressing the legislative intent.

2.1.17. Difference between Tax Evasion and Tax Avoidance

Form the view point of an ordinary person or an economist, tax evasion and tax avoidance are same. It is so because both of these activities reduce the tax liability by unethical means. But from the viewpoint of a lawyer, tax evasion and tax avoidance are different things because tax evasion is totally illegal whereas tax avoidance is done with legal backing. They are not independent but a substitute for each other since both are the means of reducing taxes and awareness of one induces a person to follow the other. According to Danis Healy, "The difference between tax avoidance and tax evasion is the thickness of the prison well."

In the country where enterprises are relatively of small size, people are relatively poor and tax morale is relatively low, taxpayers use evading practices. In contrast, in a country where business houses are relatively wealthy, taxpayers are discipline is relatively strict and people are relatively wealthy, taxpayers are more inclined to tax avoidance. In essence, tax evasion is more common in developing countries whereas tax avoidance is usual in the developed world.

To conclude, both the tax evasion and tax avoidance reduce tax liability of the government by unethical means one is done legally whereas another is illegal.

2.2. Review of Literature

System of income tax in Nepal starts from 1959 through economic act. Various studies have been carried out and article, books and researches have been written and published on different aspects of income tax in Nepal. Some of conclusion and summary of literature about income tax reviewed during this study are given in the following paragraph.

Mr. Kedar Bahadur Amatya (1965) prepared a book, "Nepal Ma Aayakar Ko Byabastha" analyzing the legal aspects and description of income tax system of that period. This is the first published book on income tax.

Mr. Govinda Lal Shrestha (1967) has prepared a Masters Degree thesis entitled "Income tax in Nepal". He has described about historical background, income tax act, rules and administrative aspects but has not shown problems related to income tax.

Mr. George E. Lent (1968) has presented a report entitled, "Survey of Nepalese Tax Structure" to IMF, Fiscal Affair Department. He has critically analyzed the scope of income tax, tax structure, taxable income exemption and allowances in Nepal at that time. He has suggested to reform income law and administration to increase government revenue through income tax. He has also

suggested to increase income tax rate at lower taxable income and to reduce at intermediate income bracket.

Mr. Narendra Lal Kayastha (1974) has tried to analyze the contribution of income and property taxes to overall revenue collection of Nepal. He has also studied history, legal and administrative aspects of income tax system in Nepal and pointed out some drawbacks such as income tax evasion and greater role of indirect tax in national revenue.

Mr. Kedar Bilas Pandey (1978) has discussed about legal aspect, structure, role, problems etc related to income tax and Economic effect of income tax in Nepal. He has found income tax playing significant role in economic development of Nepal. His study shows that income tax contributed 4% to tax revenue and per capita burden of income tax was only Rs. 0.2 in 1962/63. Contribution of income tax increased to 10% of tax revenue and Rs. 7 per capita income tax burden in 1975/76. He has also pointed the significant role of indirect tax in total revenue. The major problems in taxation, according to him were lack of scientific record keeping, lack of maintaining accounts by tax payers, lack of coordination between tax departments and revenue department, leakage in personal income tax collection. He has suggested to bring capital gain and bank interest into income tax net, to make scientific income tax accounting assessment and collection procedure, to scrap the system of income tax holiday to industries etc.

Mr. Govinda Ram Agrwal (1978) has provided details information in various aspects of income taxation in his report entitled " Resource Mobilization for Development: The Reform of Income Tax in Nepal". His study is the first comprehensive study in taxation of Nepal. The study has covered period of nine years from 1967 to 1976. The nine chaptered research shows picture of resource gap of Nepal in its first chapter. Fiscal policy, effective tax system, role of income tax, legal and administrative aspects, historical background of income tax etc. have been also discussed. He has presented various mathematical calculations such as per capita burden of income tax, buoyancy

coefficient and elasticity coefficient of income tax etc using the double log linear model. He has identified the major problems as inefficiency of tax administration and income tax evasion. He also identified tax authorities are insufficient in enforcement of law and there are not integrated programs for taxpayers' education, assistance, guidance and consulting. All things stated in research are not fully relevant today.

Mr. Purushottam Subedi (1982) has analyzed about the role on national revenue, legal aspect and historical background of income tax in Nepal. He has examined the growth of income tax collection, its ratio to GDP, cost of income tax collection and elasticity. He has pointed out tax evasion, inefficient tax administration and dominating role of indirect tax as major problems and suggested to reform tax administration.

Ms. Naina Nepal (1983) has examined origin, meaning, existing position, role, problems and future prospective of the income tax in Nepal. Inefficient income tax administration, mass poverty, lack of tax consciousness, low numbers of tax payers, lack of coordination between taxpayers and department, narrow coverage, assessment deficiency were analyzed as major problems by her. She has suggested to separate exemption limit for family and couple and to make elastic, scientific and progressive tax rate and exemption limit.

Mr. Shambhu Nath Regmi (1986) prepared a dissertation with the objective of examining the trend of income tax in Nepal, ascertaining the share of income tax to total tax revenue and its ratio to GDP. He has concluded that income tax can check the inflationary trend of country and it also directs the flow of resources of the economy into useful and productive channels and increases the productive capacity of the economy. He has suggested for precise and clear tax law, widening tax coverage, scientific method for accounting assessment and collection of income tax, easy and simple procedure for tax payment, establishment of research unit and public awareness.

Mr. Chudamani Siwakoti (1987) has especially analyzed the Income Tax Act 1974. He has described the role of income tax as economic growth, equitable distribution and stabilized growth. The major problems identified by him are evasion at high level, delay in assessment, nominal share of income tax, lack of public awareness, complicated act, untrained and inexperienced administrative personnel, lack of training and development opportunities and unevenly distributed workload to personnel. There is also high use of best judgment assessment method, no compulsion to maintain books of account and auditing accounts of all type of business, ineffective use of fines and penalties, no provision of tax review commission, no provision of sales promotion out of country and lack of weighted deduction. He has suggested for progressive tax, honest and efficient tax administration, research unit in tax offices and penalties for not maintaining accounts. He has recommended for provision of weighted deduction and reduce time limit for assessment.

Ms. Shanti Baral (1989) has tried to shown the contribution of income tax on the structure of government revenue in Nepal. She found that total revenue, total tax revenue and direct tax revenue have an increasing trend in Nepal but in unsatisfactory rate. She has found that contribution of direct tax has been decreasing and that of indirect tax is increasing each year. Exemption in agriculture income is other reason for less collection of revenue. In her study, inefficient tax administration, unconsciousness of tax payers, lack of scientific method of tax assessment and collection have been identified as the major reasons for tax evasion at high level. She has suggested that the tax administration should be honest and efficient, tax evaders should be punished, there should be scientific method for tax collection, administration cost should be minimized, research unit should be established and delays in assessment procedure should be reduced.

Mr. Hari Bahadur Bhandari (1994) has tried to examine historical background, tax structure in Nepal and contribution of income tax to economic development of Nepal. He has stated that actual collection of revenue through

income tax was lower than its estimated target. It was due to poor tax paying habit of Nepalese tax payer, poor tax paying system and spread evasion of income tax. He has suggested making effective personnel management, tax education and better public communication system, to revise and restructure exemption limit and to reduce tax collection cost.

Mr. Rup Bahadur Khadka (1994) published a Book "Nepalese Taxation: A Path for Reform". The book is divided into seven chapters: the general economic condition of Nepal, commodity taxes, income taxes, property taxes, local taxation, tax administration, and the strategy for tax reform respectively. He had analytically described about development, existing structure, main problems and possible direction of reform of income tax. He had identified the major problems of income tax as narrow coverage, unscientific tax assessment and collection, defective system from the perspective of international taxation. He has also pointed out weak tax administration, imbalance and inadequate organizational pattern, inadequate physical and other facilities, inadequate tax training, predominance of low level non technical posts, debatable scope of revenue investigation department, lack of information system. He has suggested for extension of tax coverage, scientific method of tax assessment, extension of withholding tax, inflation adjustment etc. He has also suggested to administration for reorganize and expansion, integrated information system, research unit, strengthening the revenue service etc. This book was analytical and useful to know different aspects of income tax.

Mr. Sanjaya Acharya (1994) has identified the contribution of individuals to be greatest to income tax revenue followed by public enterprises, remuneration, house rent and interest tax, semipublic enterprises and private corporate bodies respectively in his study period. He has recommended simplifying the tax structure, legal and administrative aspect. Exemption limits for remuneration and business individual should be different according to him.

Mr. Shiva Narayan Shahu (1995) has studied on Nepalese tax structure, role and contribution of income tax on national revenue. He has identified that 0.35

percent of total population came under categories of tax payer. Income tax has been gradually increasing and was in fourth place in the tax structure of Nepal. He has not discussed the major aspects of income tax clearly and analytically and the study is not fully relevant today.

Mr. Krishna Kumar Shakya (1995) has tried to analyze the causes of heavy reliance of indirect taxes, to analyze volume of indirect tax revenue and direct tax revenue in total tax structure, highlighting the revenue assessment procedure from different sources and suggesting for improvement. He has identified that income tax has occupied fourth position among tax revenue following custom duty, sales tax and excise duty. He has mentioned Nepalese taxable capacity is limited by various factors such as low per capita income, extensive subsistence economy, relatively closed economy, political and social factor, weak export position and administrative and enforcement problems of tax department. He found that the ratio to GDP, total revenue, total tax revenue and direct tax revenue have been increasing in Nepal but in very low rate. Tax evasion is the main reason for this. Lack of clear and comprehensive definition of income, lack of punishment to the evaders, low tax paying capacity and non conscious of tax payers, lack of inefficient tax administration, lack of scientific method of tax collection and lack of trained tax collectors were the main reasons of tax evasion, He has suggested increasing efficiency of income tax. His major recommendations were assessment of small tax payers should be on a door to door basis, self assessment of tax should be encouraged and salary as well as income tax exemption line should be tied up with the cost of living index. The study was based on old income tax act. **Mr. Kamal Deep Dhakal (1998)** published a modified edition of book named "Income tax and house and compound tax law and practice with VAT". He has described historical aspects and legal provisions related to income tax and presented methods of income tax assessment with numerical examples, This book was fully based on the syllabus of BBS third year and MBS second year and was published before coming new income tax act 2002. The book is very useful to know the general information and legal provision of income tax act 1974. His book is

informative rather than analytical. Revenue Consultation Committee Report (2001) has emphasized to simplify the tax policy to increase voluntary compliance. The report has recommended for written communication between taxpayer and tax administration rather than the informal relation and has suggested to widen the income tax base by including all kinds of taxpayer and income and to find out the taxpayers of new sector. Suggestion has provided to make the act more transparent and clear to attract foreign and domestic investor for this purpose. The report also has suggested increasing income tax exemption limit with considering purchasing power and inflation rate.

Dr. Poudyal (1998) has presented the provision under income tax act in detail and definition of corporate tax structure in Nepal in his book named, "Corporate Tax Planning in Nepal." This book is also provides a comprehensive information to managers for tax planning under the framework of Income Tax Act 1974 and Industrial Enterprise Act 1992. It also pinpoints the areas where tax implications are either ignored or are given less importance in decision making by the managers. The study is, thus, expected to benefit corporate planners, entrepreneurs, managers, tax authorities and the academician. Moreover, no study on corporate tax planning has so far been conducted in Nepal. This study therefore fills in these important gaps in the areas of corporate taxation.

Ms. Bhibha Pradhan (2002), in her study of contribution of income tax from public enterprises to public revenue includes historical background, contribution of income tax to the public revenue, contribution of Nepal Telecommunication Corporation to income tax, effectiveness of income tax collection. She has found that the contribution of income tax from public enterprises in Nepal was not significant due to poor achievement, weakness in government's economic policy and deficiency in legislation. NTC has been contributing effectively to total income tax revenue. Average contribution of income tax from NTC to total income tax revenue, total direct tax revenue, total tax revenue, and total government revenue was 15.06 percent, 2.37

percent, 11.1 percent and 1.93 percent respectively in average in 1998/99. She also found that contribution of tax revenue on GDP of Nepal was lower than other SAARC countries except Bangladesh. Her suggestion for income tax system were clear cut provision, discretionary power of tax officers should be curtailed, assessment and collection provision should be made clear and simple, provision of reward, prize, incentive should be introduced to encourage the taxpayers to pay voluntarily, compulsory provision of auditing etc. She has also suggested promotion and rewards to active, efficient and honest tax personnel; tax education to tax payers; strict actions against corruption; reduction of delays in tax assessment for the improvement of income tax administration in Nepal.

Mr. Vidyadhar Mallik (2003) has published a book "Nepalese Modern Income Tax System" with twenty six chapters and eight annexes. He has described historical aspects of income tax, changes brought by the Income Tax Act 2002 and the development of income tax management in Nepal. He has also described different legal provisions relating to Income tax with numerical examples. The book is very useful to know the general information and legal provisions of new Income Tax Act. His book was informative rather than analytical. He has not analyzed the role of income tax, structure of income tax in Nepal.

Dr. Pushpa Raj Kandel (2003) published a book named "Tax Laws & Tax Planning in Nepal". The book is based on new syllabus of BBS and MBS. It has five parts, sixteen chapters and seven annexes on basic concept, provision of income tax act 2002, tax administration, house and land tax, VAT, tax laws and tax planning etc. The book is more informative rather than analytical.

Mr. Dan Bahadur Palli Magar (2003) has concentrated on the exemption and deduction provision of income tax law. He has found that there was a dominated share of tax structure in Nepalese government revenue. He found the contribution of direct tax and indirect tax to be 25.56 percent and 74.44 percent of total tax revenue in 2001/02. Income tax has occupied third position

on the basis of mean contribution among sources of revenue and is in increasing trend. The tax GDP ratio was not found satisfactory. With income tax, corporate income tax is in first position with dominating role and in decreasing trend while income tax from individual is occupying second position and is in increasing trend. He has stated the major causes for inefficient tax administration as lack of trained employees, shortage of income tax experts and professionals in tax administration, lack of public participation, faulty organizational structure of tax administration, weakness in government policy and defective income tax act. He has suggest for revision the exemption limit, elimination double taxation in dividend, tax rebate for submitting true income statement in time, increase income tax rate slab up to 10, increase exemption limit to individual as well as family, special package for industrial development in remote area, tax provision for agriculture income above some specified exemption etc. His major suggestions about deduction are clear provision for deduction, fully allowed interest expenses, pollution control expenses, repair and improvement expenses and research and development expenses. His study has covered exemption and deduction provision of income tax laws. He has not mentioned other various aspects of income tax.

Mr. Sushil Kumar Dahal (2005) has studied with the objectives of analyzing contribution of income tax and volume of indirect and direct tax, examining the effectiveness of income tax revenue collection, knowing view of tax payer tax experts and tax officers about various aspects of income tax and to recommend possible measures. His study has covered introduction, conceptual framework and legal provision, presentation of different data related to income tax, empirical study and summary conclusion and recommendations. His major findings are: There is dominant role of tax revenue in Nepalese government revenue, but is in decreasing trend. It was 85.2 percent in 1982/83 and is 78.0 percent in 2001/02. Average contribution of direct and indirect tax in his study period is 20.63 percent and 79.40 percent respectively. The resource gap is in increasing trend and tax GDP ratio is not found satisfactory. Income tax is the important source of internal revenue and occupies third position after costume

duty and VAT. He has found income tax from individuals to be occupying first position but with decreasing trend. He has also stated that mass poverty and low income level, increasing habit of tax evasion, inefficient income tax administration are the major reasons for low contribution of income tax and lengthy process, vague provisions of income tax laws consuming unnecessary time, lack of awareness are major problems facing by tax payers. He has made some recommendations. Tax ratio should be gradually increased to adopt principle of ability; Income tax policy should be timely revised by income tax experts following economic policy of nation; Income tax rules and regulation should be clear and simple; rate of fines and penalties should be increased; a research and intelligence centre should be established in each tax office, tax personnel and tax payers should be encouraged as well as punished for their works; separate income tax department should be established; income tax net should be broad by bringing house and land rent, doctors' clinic, consultancy service, tuition, research etc into income tax net are the major recommendations made by him.

Besides these books and dissertations some reports and articles published in different newspapers and magazines and government publications such as budget speech, economic survey, national plan etc were reviewed during the study period. This dissertation is expected to be focused on current situation of income tax system.

2.2.2. Review of Reports, Articles and Journals

Mr. Timsina (1978), wrote a thesis entitled, "**Income tax evasion in Nepal**" the objective of his study, were to analyze the structure of income tax in Nepal, to study the role of income tax in mobilizing resources in Nepal, to examine income tax evasion tendency in Nepal, to observe the general opinion about income tax evasion in Nepal. He has shown serious problem of finance resource gap in Nepalese Economy. He has stated that income tax evasion tendency by remuneration tax payers are increasing in Nepal. He has pointed out different cause of income tax evasion in Nepal viz widespread illegal

business, high corruption, poor tax paying habits inefficient tax administration, open border with India and political indiscipline in Nepal. He has also mentioned different method of income tax evasion in Nepal viz, non reporting of income from illegal business, non mentioned of accounts, failure to submit income statements, non reporting of family members incomes, under reporting of income from different sources, re- registration of business and failure to make deduction at source (TDS). He has concluded that income tax evasion is in decreasing trend in Nepal. But due to lack of complete and authentic data, he was unable to prove it statistically.

Mr. M.K. Dahal et.al. (1995), presented and submitted a report entitled "**Review of Tax System**" to MOF, Gon. covered the various aspects of tax system at that time. Narrow tax base elasticity, higher burden of indirect tax to direct tax, lack of voluntary compliance, leakage etc were the major defect of taxation identified by this report. This study stressed on the narrow tax base. The exemption of income from agriculture sector, which contributed 43% of total GDP was marked as a main reason of narrow base including agriculture sector, income from domestic industries, social sector and electricity sector that contributed 52% was exempted from Income Tax and only large industries, mines, construction, trade, hotel and restaurant that contributed 48% income to GDP were under income tax. All these provisions made the tax base very low. The tax rates were unnecessarily high. Only 73000 tax payers was demarked which was less than one percent of economically active population. Real per capita income growth rate at that time was only 0.3 percent, which showed the low taxable capacity of people. This report suggested increasing the tax to GDP, to increase the total number of taxpayers and to increase the per capital income. This study further suggested about 40 percent extra resource mobilization, it propose tax policy and program were in pace. This study recommended various practical ideas to widen income tax base like 20 percent exemption form total tax assessment effective. It also suggested the exemption limit should be raise based on inflation rate.

Miss Pradhan (2001), published a thesis "**Contribution of Income Tax from Public Enterprise to Public Revenue of Nepal with Reference to Nepal Tele Communication Corporation.**" She has analysed the contribution of income tax from public enterprises, shown the contribution of income tax in total tax and total income tax revenue of Nepal, analyzed the effectiveness of Income tax revenue of Nepal, and analyzed the effectiveness of income revenue collection from NTC. She has also recommended possible measures to increase the present status. She has found that contribution of income tax from PEP in Nepal is not satisfactory due to poor achievement weakness in government's economic policy and deficiency in legislation. Existing corporate tax rate has been found suitable. Self assessment of tax is more appropriate. Public enterprises have remained in the second place on total income tax revenue. Out of PES, NTC has contributed effectively to total income tax revenue of Nepal. NTC's contribution to total corporate income is high. She has found that the average share of NTC on corporate income tax was 35-76 during ten years period i.e. from fiscal year 1989/90 to 1998/99. She has recommended possible measures to overcome the existing problems. Staff should be taught discipline and be motivated. Management should have the feeling to contribute to the state etc.

Mr. Gautam (2004), has described about, "**Contribution of income to national revenue of Nepal.**" He has mainly focused about conceptual framework, legal provision and structure of income tax. He has conducted an empirical investigation about various aspects of income tax in Nepal.

He has found that contribution of direct and indirect tax revenue were 20.63 percent and 79.04 percent respectively in 2002/03. Income tax revenue has occupied third position based on mean contribution other sources of revenue; the contribution of income tax to total revenue was 8.84 percent. It may enhance the revenue of government promote to distribute justice and encourage private sector investment. Nepalese government expenditure is increasing at the faster rate than the increase in revenue. The resource gap has existed in Nepalese

economy and it is in creasing trend, tax/ GDP ratio of Nepal is found satisfactory, the exemption limit is not satisfactory. He has mode the specific suggestion for a sound and effective in income tax system. They were establishment, promotion and reward system to efficient and honest tax personnel, increasing public participation to minimize the tax evasion, strict action against corruption, income tax, rules and regulation should be clear and simple. The provision of times, penalties and punishment should be mode at higher rate for income tax evaders; more deduction should be provided for exports promote and separate income tax department should be established.

CHAPTER - III

3. RESEARCH METHODOLOGY

Methodology part of every research work serves as the bridge linking two edges of river. It is the road map of every research work whether scientific or applied research. It suggests every researcher to get the easy and efficient destination achievement stated in research objectives.

3.1. Types of Research

This study includes three types of research as descriptive, analytical and empirical.

3.2 Research Design

The research study is focused on role of income tax and composition of income tax revenue and its trend before and after enactment of Income Tax Act 2002 in Nepal. To achieve the stated objectives, data has presented and analyzed from different sources. An opinion survey is carried out with 60 respondents associated with different denomination related to income tax i. e. tax experts, tax administrators and tax payers. The opinions were collected through structured questionnaire. The questionnaire included the role of income tax, effectiveness of income tax system, trend of income tax and reason, suggestion to reform income tax system, most important factors of new act etc. Thus, the study is descriptive, analytical and empirical.

3.3. Population and Sample:

All the tax experts and employees in Nepal are considered as total population. The tax expert, income taxpayers and administrators in Nepal are considered as target population. To fulfill the objectives of the study, 60

samples size is selected from different denomination. Persons selected for empirical study are carefully selected by consultation with lecturers and best judgment method. The respondents are from three groups. The group of respondents and size of sample is stated in table 3.1.

Table 3.1

Group of Respondents and size of samples

SN	Group of Respondents	Sample Size
1	Income Tax Experts	20
2	Income Tax Administrators	20
3	Income Tax Payers	20
	Total	60

3.4. Nature and Sources of Data:

The data collected to describe this study are from two sources i.e. primary and secondary. The major sources among them are stated below:

1. Primary Data:

To know the views of different persons related to income tax, an opinion survey is carried out through structured questionnaire to sample population. The questionnaire was same for all the respondents. The persons involved in survey are from different parts. Tax administrators are from IRD and various sectors of tax offices. Tax experts are the lecturers, auditors, CAs etc. Selection of tax payers is made from various sectors manufacturing, service, trading, financial etc.

2. Secondary Data:

The comparative progress study and other basic analysis of study is made by secondary data. The sources of secondary data during this study are:

- i. Economic Survey of various years, Ministry of Finance, Govt/Nepal.
- ii. Budget Speech of various years, Ministry of Finance, Govt/Nepal.
- iii. Reports of Internal Revenue Departments of various years.
- iv. Different books related to income tax and public finance.
- v. Dissertations related to income tax.
- vi. Different Newspapers, journals, souvenir, magazines.
- vii. Websites of different organizations such as World Bank, IMF, MOF, IRD etc.
- viii. Other relevant records and data.

Secondary data from FY1991/92 to 2005/06 has been used in this study.

3.5. Data Collection Procedure:

All the data from secondary sources are collected through reliable sources as accurate as possible by researcher and has to visit different offices, libraries and book stalls for this purpose. The primary data is collected by distributing and collecting questionnaire from different location and help of different people is taken during the process.

3.6. Data Processing and Analysis Procedure:

Collected data from various sources are thoroughly reviewed and sorted on the basis of their homogeneous nature and resemblance of the facts. The sorted data are arranged and presented systematically in suitable tables. The processed and tabulated data were analyzed through different statistical tools

such as percentage, simple average, graphs, tables, charts etc for clear and systematic presentation of findings.

3.7. Limitation of Methodology

All research study is to be done to solve particular research problems. It requires various kinds of data materials and other relevant information, which cannot sufficient to the researcher. This study cannot escape from the frame of limitation, this study mainly base on secondary data as well as primary data.

-) The methodology is followed in this study is not designed by advanced and sophisticated technique.
-) Also non availability of plentiful literature on the subject has handicapped the study to some extent.
-) This study is only in corporate sector of Nepal.
-) Times and resources constrains may limit the area covered by study.
-) This study is mainly based on published secondary data and information related to corporate tax as made available by NRB tax office and Minister of Finance from last five year published data.

CHAPTER - IV

4. DATA ANALYSIS AND PRESENTATION

4.1 Data Presentation and Analysis

Data Presentation is devoted to the analysis and presentation of secondary data as well as primary data. The secondary data have been obtained from economic survey, economic bulletin, budget speech and other related newspaper. The primary data have be obtained from fill the questioners and asking questions. The available data have been tabulated and presented into graphs, charts and analyzed to reach at some findings.

4.1.1. Structure of Total Tax Revenue in Nepal

Nepal's public economy is suffering from low revenue performance and growing public expenditure. The basic sources of revenue are tax revenue and non tax revenue but collection of these revenues is not sufficient to cover expenditure. The composition of tax revenue and non tax revenue from FY 2002/03 to 2006/07 is presented in table 4.1. This shows the dominated role of tax revenue as 75.74 percent of total revenue in 2002/03 and 77.36 percent in 2006/07. Share of non tax revenue for the same period seems to be 24.26 percent and 22.68 percent respectively. The amount of tax revenue is continuously increasing but that of non tax revenue is fluctuating, that's why the share of tax revenue and non tax revenue are not uniform. The tax revenue seems to be 79.45 percent as maximum and 75.74 percent as minimum contribution to national revenue in 2005/06 and in 2002/03 respectively within the study period.

The tax revenue contributed amount of 42587.0 million and 63542.20 million in 2002/03 and in 2006/07 respectively. Figure 4.1 shows that the increase is generally in constant rate. The contribution of non tax was 11115 million and

18593.10 in subsequent fiscal years. Composition of tax revenue and non tax revenue is shown in figure 4.1.

Table No. 4.1

Structure of Total Tax Revenue in Nepal

In Million

Fiscal Year	Total Revenue	Tax revenue		Non-tax Revenue	
		Amount	Percentage	Amount	Percentage
2002/03	56229.8	42587.0	75.74	13642.7	24.26
2003/04	62331.0	48173.0	77.29	14158.0	22.71
2004/05	70122.7	54104.7	77.16	16018.0	22.84
2005/06	72282.1	57430.4	79.45	14851.7	20.55
2006/07	82135.30	63542.20	77.36	18593.1	22.63

Source: Economic Survey 2006/07. Economic Bulletin,

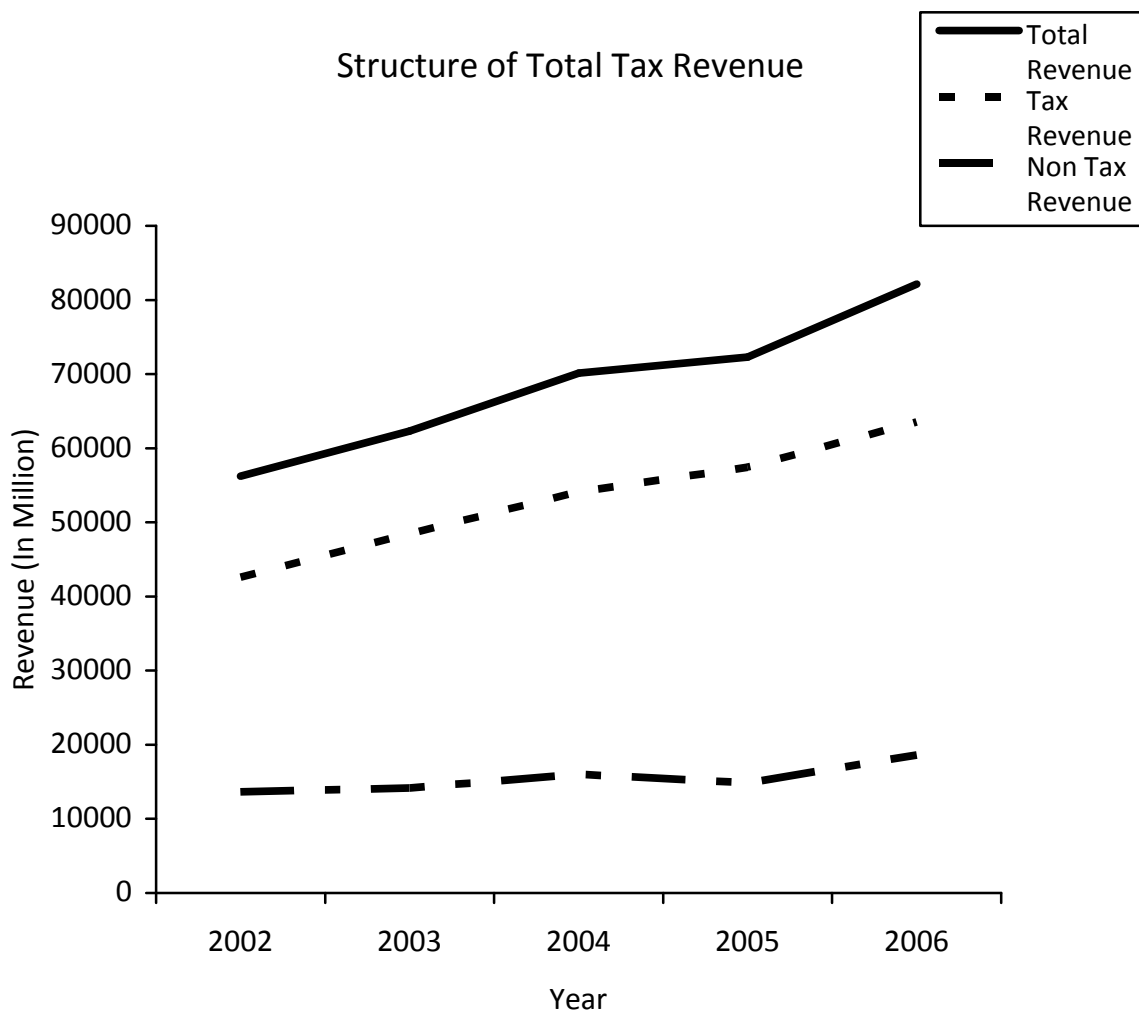


Figure 1

4.1.2. Composition of Tax Revenue in Nepal

Tax revenue is the major source of government. In Nepal contribution of tax revenue is about 80 percent. It is the tools to mobilize internal resources effectively. The tax revenue constitutes direct and indirect tax. Direct tax includes income tax, land and revenue and registration, urban house and land tax, vehicle tax and indirect tax generally includes costumes, VAT, excise.

The share of direct tax and indirect tax in total tax revenue is presented in figure 4.2. This shows the increasing trend of both direct and indirect tax. Indirect tax has a leading role in total tax revenue up to 76.44 percent within

the study period. Although the amount of indirect tax is increasing, its share to total tax is decreasing. Its share was 76.27 percent in FY 2002/03 and reduced to 75.27 percent in 2003/04 and gradually increased to 75.84 percent in 2004/05. In the other hand direct tax has an increasing trend. Its share became 23.55 percent in 2006/07 from 23.73 percent in 2002/03. The mean contribution of direct tax and indirect tax to total tax revenue are 23.95 percent and 76.05 percent within study period.

Table 4.2

Composition of Tax Revenue

In Million

Fiscal Year	Total Tax Revenue	Direct Tax Revenue		Indirect Tax Revenue	
		Amount	Percentage	Amount	Percentage
2002/03	42587.0	10105.8	23.73	32481.2	76.27
2003/04	48173.0	11912.6	24.73	36260.4	75.27
2004/05	54104.7	13071.8	24.16	41032.9	75.84
2005/06	57430.4	13968.1	24.32	43462.3	75.68
2006/07	63542.20	14968.1	23.55	48574.10	76.44

Source: Economic Survey 2006/07

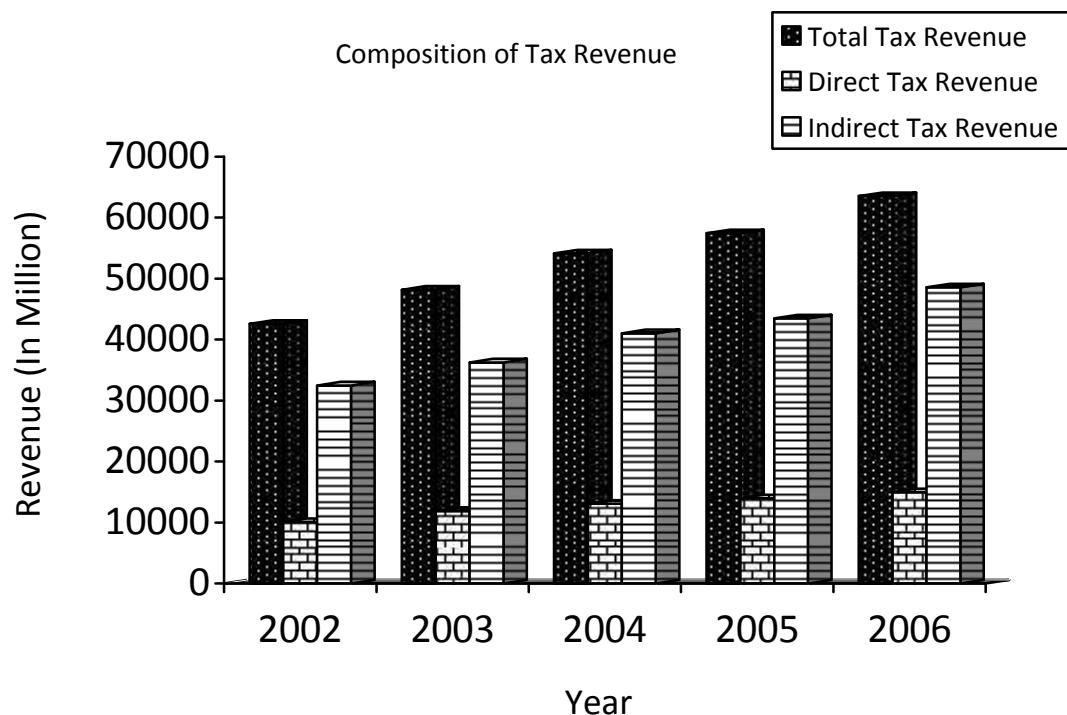


Figure 2

4.1.3. Composition of Income Tax

Income tax is the major source of direct tax revenue. It was first introduced as business profit and remuneration tax in 1959/60 in Nepal. It contributed only 203 thousands in that FY. It reached 10373.7 million after 46 years in FY 2006/07 which is out of range of compare. The income tax collection in different income years are shown in table 4.3.

Total Income tax is increasing each year. The amount from income tax was only 7966.2 million in 2002/03 and its increase is optimistic up to 2003/04 while it reaches to 9245.90 million. Its trend is gradually increasing after this within study period.

Income tax constitutes Income tax from public enterprises, semi public enterprises, private corporate bodies, individual, remuneration and tax on

interest. The share of these different sources in percentage is shown also presented in table 4.3.

The table shows that role of income tax from public enterprises is significant. It has contributed 21.2 percent to total income tax in average. The trend of income tax from public enterprises is fluctuating. It was 1251 million in 2002/03 and gradually rises up to 2056.6 million in 2003/04. Its maximum and minimum shares were 22.2 percent and 15.7 percent in 2002/03 and 2003/04 respectively. Then after its trend is increasing. The share of income tax from private corporate bodies is 19.5 percent in average. It was in increasing trend up to 2002/03 from 10.8 million. It also declines for next years.

Table 4.3

Composition of Income Tax Revenue

F/Y	Total Income Tax Revenue	Public Entrepreneur	Private Corporate bodies	Individuals	Remuneration.	Interest on Tax
2002/03	7966.2	1251.0	1236.3	3362.3	1252.6	864.0
2003/04	9245.9	2056.6	1531.3	3533.4	1391.2	733.4
2004/05	10159.4	1332.4	2467.8	3926.3	1675.9	757.0
2005/06	10373.7	195.7	3404.3	4234.7	1764.1	565.7
2006/07	11373.7	595.7	3804.3	4534.7	1773.3	665.7

Source: Economic Survey 2006/07. Ministry of Finance and Economic Bulletin,

Table 4.3

Composition of Income Tax Revenue

F/Y	Total Income Tax Revenue	Public Entrepreneur	Private Corporate bodies	Individuals	Remuneration.	Interest on Tax
2002/03	100.0	15.7	15.5	42.2	15.7	10.8
2003/04	100.0	22.2	16.6	38.2	15.0	7.9
2004/05	100.0	13.1	24.3	38.6	16.5	7.5
2005/06	100.0	1.9	32.8	40.8	17.0	5.5
2006/07	100.0	5.32	33.44	39.87	15.59	5.85

Sources: Economic Survey 2007

Composition of Income Tax Revenue

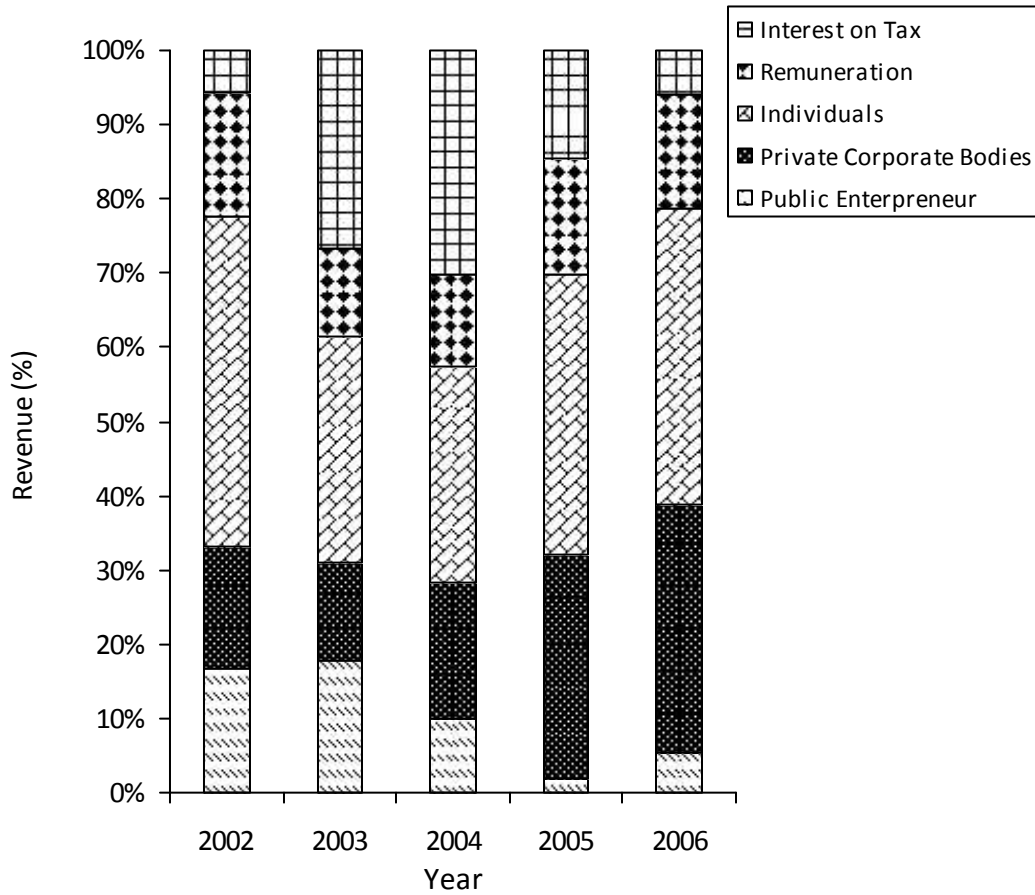


Figure 3

4.1.4 Contribution to GDB

Table 4.4 shows the contribution of income tax to GDP. The contribution of income tax to GDP in FY 2002/03 was just 1.89 percent. It was continuously increasing rapidly up to 2003/04 and reached at maximum level of 2.27 percent. It cannot be continued for the following period of new act and started declining. It declined to 2.19 percent in 2005/06 and again to 2.18 percent in 2006/07.

Table 4.4

Contribution to GDP

In Million

Fiscal Year	Total Income Tax Revenue	Percentage of income tax to GDP
2002/03	7966.2	1.89
2003/04	9245.9	2.16
2004/05	10159.4	2.27
2005/06	10373.7	2.19
2006/07	11373.7	2.18

Source: Economic Survey 2007

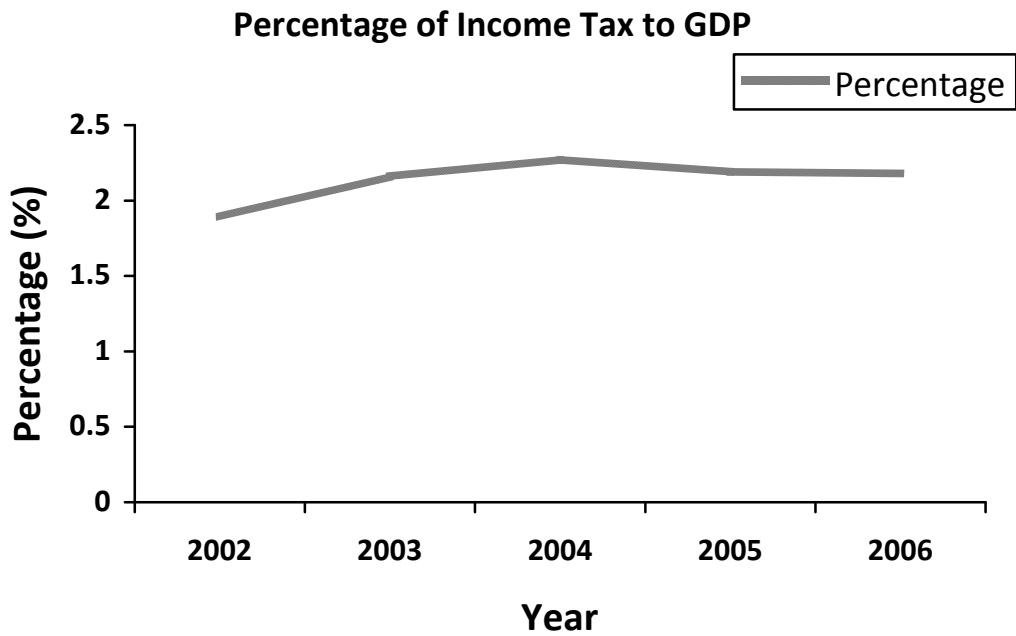


Figure 4

4.1.5 Contribution to Total Revenue

The contribution of income tax to total revenue was 6.48 percent in FY 1991/92. It is positively correlated with time up to 2000/01. Its share in 2000/01 was 18.64 percent. It declines for next two years to 17.65 and 14.17 percent. It gradually increased for 2003/04 year to 14.83 percent and again decreased to 14.35 and 13.84 percent for last two years. The contribution of income tax to total revenue is shown in table 4.5.

Table 4.5

Contribution of income tax to total revenue

In Million

Fiscal Year	Total Income Tax Revenue	Total Revenue	Percentage of income tax to total revenue
2002/03	7966.2	56229.8	14.17
2003/04	9245.9	62331.0	14.83
2004/05	10159.4	70122.7	14.49
2005/06	10373.7	72282.1	14.35
2006/07	11373.7	82135.30	13.84
Total	49118.90	343100.90	14.32

Source: Economic Survey 2007

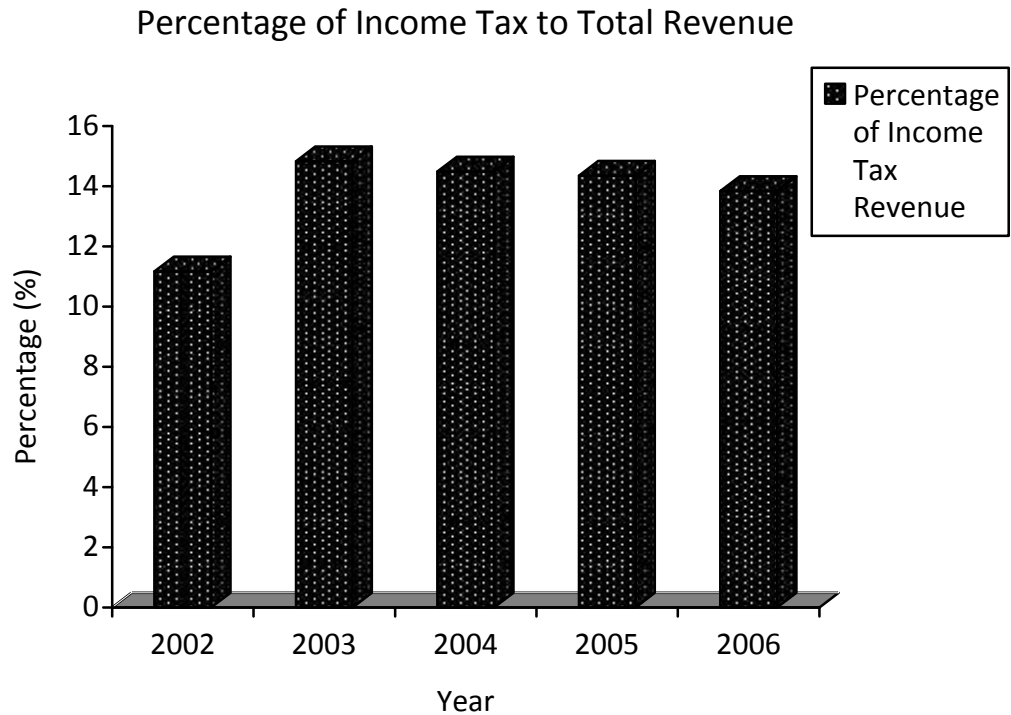


Figure 5

4.1.6. Structure of Corporate Tax Revenue in Nepal

Corporate tax revenue plays the vital role contribution on Government Revenue collection. It is not only a collection on government revenue but also a development of country. In the source of collecting of government revenue of corporate sector there are four main sources which is government corporation, Public Ltd. Company, Private Ltd. Company and Income from other institution. Here is shown in the table 4.7.

Table 4.6

Structure of Corporate tax Revenue in Nepal

Rs. In Million

Corporate Sector	2002/03	2003/04	2004/05	2005/06	2006/07

Government Corporation	27499.4	33732.8	39761.9	1549.2	3284
Public Ltd. Corporation	5118.9	10783.2	8476	15779.7	24560.7
Private Ltd. Company	11746.8	11887.8	19228.8	18305.6	22551.8
Income From Other Institution	10107.8	10457.6	10353.1	1604.3	1247.3

Source: Nepal Rastra Bank

Table 4.7 shows the collection of government revenue in different corporate sectors. In the F/Y 2002/03 Government Corporation bodies Rs. 27499.4 million, Public Ltd. Company Rs 5118.9, Private limited Company Rs. 11746.8 and Other Institution Rs 10107.8. It is also shown in the higher position occupied in government corporation bodies from collection of government revenue. Private Ltd. Company occupied in second position in this year. In the F/Y 2003/04 and 2004/05 collection of government revenue is increasing in Government Corporation then after decreasing in F/Y 2005/06 and 2006/07. Public Ltd. Company is also increasing in F/Y 2003/04 and decreasing in F/Y 2004/05 then after increasing in F/Y 2005/06 and 2006/07. Private Ltd. Company is increasing in year 2003/04 and 2004/05 and decreasing in 2005/6 than after increasing in collecting government revenue. Other Financial Institution is also same in Private Ltd. Company.

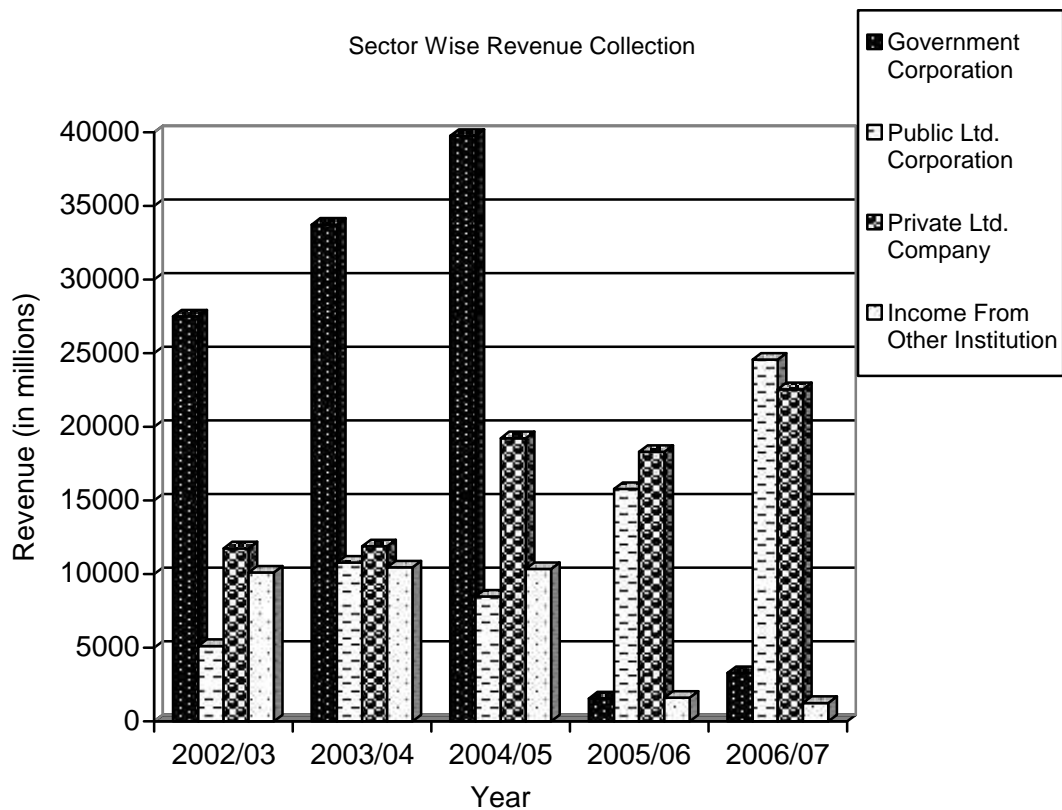


Figure 6

In the figure, Government Corporation contribution on Government Revenue is increasing in F/Y 2002/03, 2003/04 and 2004/05 then after decreasing F/Y 2005/06 and 2006/07. Fiscal year 2005/06 Private Ltd Company occupied in first position collecting in government revenue and Public Ltd. Company occupied in second position collecting in government revenue. Similarly Government Corporation and Income from Other Financial Institution is fewer occupiers in collecting in government revenue in this year. In the F/Y 2006/07 Public Ltd. Company occupied in first position in collecting government revenue and second position occupied in Private Ltd. Company. It is also fewer occupiers in Government Corporation and Income from Other Financial Institutions.

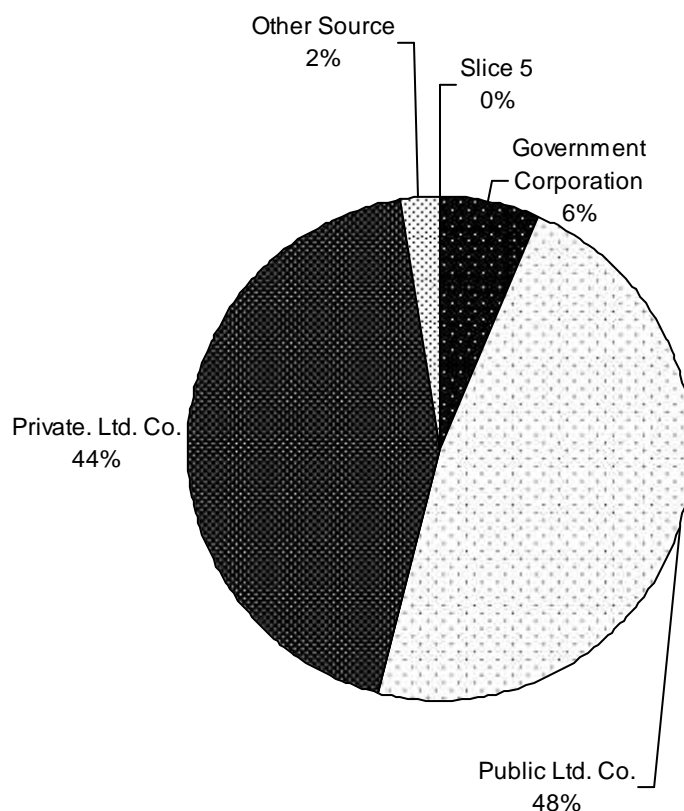


Figure 6.1

In the figure, Maximum area occupied in public corporation which is 48% then after individual and Sole Trading occupied 24% which is in second position for the year 2006/07. Then after, private ltd. Company covered in third position in the figure which is 20% area is occupied in the chart. Income from other and government corporation are also little contributed in collecting government revenue, which is shown in figure 2% and 6% respectively.

4.1.7 Structure of Government Revenue in Nepal

Nepalese Government Revenue is structure is formed by combination of corporate income tax and other tax. Corporate revenue is that revenue which

is collected in the corporate sector. In the corporate sector all of the government and non government sector are include Government Corporation, Public Ltd. Company, Private Limited Company and Income from Other Sources. Similarly other tax contribute value added tax, excise duty, custom duty, house and land registration, vehicle tax etc.

Table 4.7

Structure of Government Revenue in Nepal

In million

Year	Corporate Income Tax Revenue	Non Corporate Tax Revenue	Total Tax Revenue
2000/01	7831.2	41062.4	48893.6
2001/02	7252.3	43193.3	50445.6
2002/03	5554.0	50675.7	56229.7
2003/04	6805.0	55526.0	62331.0
2004/05	7331.3	62791.8	70123.1
2005/06	7576.6	64705.5	72282.1
2006/07	11604.9	76107.2	87712.1

Source: Nepal Rastra Bank

In the table 4.8, government revenue collection from corporate tax in different year. In year 2001/02, government revenue collection from corporate tax Rs. 7831.2 millions and other tax Rs 41062.4 millions. In this case corporate tax contribution on government revenue is less contributes in this year. Than after, year 2001/02 it is also in less contributes in government revenue here is only Rs. 7252.3 million out of 50445.6 million. In this year government revenue collection from corporate tax is decrease in previous

year. Similarly, corporation tax collection is decreasing in year 2002/03 and 2003/04 Rs. 5554 million and Rs.6805 million respectively. Fiscal year 2004/05 corporate tax collection is slowly increase in previous year. F/Y 2005/06 corporate tax contribution on government revenue is increasing in previous year because of the political situation is change in the Nepal. Normally this year is increasing on export and import goods and services. F/Y 2006/07 the corporate tax is increasing Rs. 4028.3 million in the year 2005/06. It is the highest increasing in the previous year and total revenue is little increase only because of little increasing of other sectors revenue. It is not satisfactory to collecting the government revenue. This types of the collecting the government revenue is not only a fully support in nation development but also a little role. That is why Nepal is always depending upon the foreign aids and loan. Therefore, government plays the vital role where all the corporate sector and non corporate sector are exacting to paying the tax. Tax is the main source of collecting government revenue. In the above table describe the statistical tools use coefficient of correlation.

Table 4.8

Calculation of correlation between Corporate Income Tax and Other Tax

Year	Corproate Income Tax (x)	Other Tax (y)	u=(x- 7707.9)	u ²	v = (y- 56294.56)	v ²	uv
2000	7,831.20	41,062.40	123.30	15,202.89	(15,232.16)	232,018,698.27	-1878125.328
2001	7,252.30	43,193.30	(455.60)	207,571.36	(13,101.26)	171,643,013.59	5968934.056
2002	5,554.00	50,675.70	(2,153.90)	4,639,285.21	(5,618.86)	31,571,587.70	12102462.55
2003	6,805.00	55,526.00	(902.90)	815,228.41	(768.56)	590,684.47	693932.824
2004	7,331.30	62,791.80	(376.60)	141,827.56	6,497.24	42,214,127.62	-2446860.584

2005	7,576.60	64,705.50	(131.30)	17,239.69	8,410.94	70,743,911.68	-1104356.422
2006	11,604.90	76,107.20	3,897.00	15,186,609.00	19,812.64	392,540,703.77	77209858.08
	7,707.90	56,294.56	-	21,022,964.12	(0.02)	941,322,727.10	90,545,845.18

$$r = \frac{\sum UV - \frac{\sum U \sum V}{N}}{\sqrt{\sum U^2 - \frac{(\sum U)^2}{N}} \sqrt{\sum V^2 - \frac{(\sum V)^2}{N}}}$$

$$7 \times 90545845.18 - 0$$

$$r = \frac{\quad}{\quad}$$

$$7 \times 21022964.12 - 0 \quad 7 \times 941322727 - 0$$

$$633820916.20$$

$$r = \frac{\quad}{\quad}$$

$$969680301938144000.00$$

$$633820916.20$$

$$r = \frac{\quad}{\quad}$$

$$984723464.70$$

$$r = 0.643$$

In the correlation coefficient of r is equal to +1 or -1. If r = 1 there is positively perfect correlation between the two variable and if r is equal to -1 there is perfect negatively correlated each other. If r is nearly closed to +1 the there is closely relationship between two variable. In the above calculation r = 0.634 it is not closely relationship between corporate tax income and other tax income but only related to the contribution on collecting in government. In the collection of government revenue corporate tax play the vital role in the

development of nation. But it is not found this relation which is only little area occupied in government tax revenue. In the content of Nepal, most of the corporate sector especially in Private Ltd. Company corruption the tax. In the budget speech all the corporate sectors are include the income tax rule and regulation. But the implement is not found because of the lack of knowledge of tax payers.

4.1.8 Revenue Contribution on Government Corporation

Government Corporation means those organizations which is occupied in 51 percent share in government and then run in government rules and regulation is called the Government Corporation. Government Corporation contribution on collecting government revenue plays the vital roles. In the above table it covered in the first position in collecting of government revenue from the corporate sector. These are the following in the Government Corporation; Corporate Bank (Agriculture Development Bank, Nepal Rastra Bank, Nepal Banija Bank), Security Boards, Nepal Stock Exchange, Insurance Corporation, Citizen Investment Fund and Employment Provident Fund.

Table 4.9

Revenue Contribution on Government Corporation

Particulars	2002/03	2003/04	2004/05	2005/06	2006/07
Corporate Bank	11599.7	13432.6	15395.5	549.6	1238.3
Security Board	7130.3	10485.4	9359.1	120.7	238.9

Stock Exchange	2050.4	1275.3	3535.4	167.9	143.1
Insurance Corporation	3222.6	2150.7	2315.9	213.5	533.2
Citizen Investment Fund	1112.5	1210.4	2135.6	146.5	465.3
Employment Provident Fund	2383.9	2177.8	5220.4	351.0	668.7

Source: RB, Nepal

Government Revenue contributes in Government Corporation is shown in this table 4.10. In this table maximum Government contribute in Government Corporation is corporate banking. Corporate banking includes Nepal Rastra Bank, Agriculture Development Bank and Nepal Banija Bank. In the year 2002/03 Government Revenue Contribution on Government Corporation Rs.7449.40 which is covered by corporate banks Rs. 11599.7, Security Board Rs 7130.30, Stock Exchange Rs. 2050.40, Insurance Corporation Rs 3222.6, Citizen Investment Fund Rs 1112.5 and Employment Provident Fund Rs 2383.9. Then after, in F/Y 2003/04 Government Corporation Rs. 33732.8 which is collection from Corporate Banking, Security Board, Stock Exchange, Insurance Corporation, Citizen Investment Fund and Employment Provident Fund Rs. 13432.6, Rs. 10485.4, Rs. 1275.3, Rs. 2150.7, Rs. 1210.4 and Rs. 2177.8 respectively. Similarly, F/Y 2004/05 also collecting in Government Revenue from Corporate Sector is increasing and then after decreasing in the F/Y 2005/07 and 2006/07

Revenue Contribution From Government Corporation

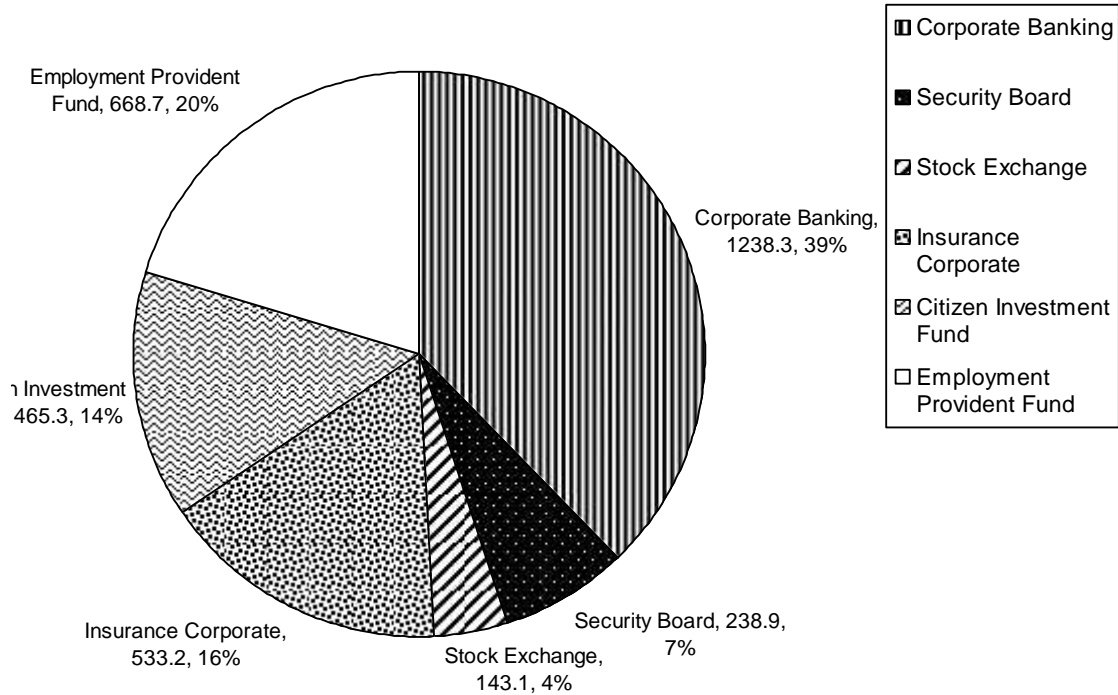


Figure 7

In the figure shown Corporate Banking Sector contribute in first position collecting in Government Revenue. Then after second position contribute in Employment Provident Fund. Third position occupied in Insurance Corporations and Citizen Investment Fund, Security Board and Stock Exchange occupied in fourth, fifth and six positions respectively.

4.2. Empirical Study

4.2.1. Introduction

An empirical survey was conducted to know the different aspects of income tax in Nepal. The structured questionnaire was prepared and distributed for this purpose to collect opinions of respondents. The questionnaire has covered role of income tax, features of new act, condition of income tax system and administration in Nepal and suggestion for betterment of income

tax system in Nepal. (Appendix A). The respondents were personalities from different field categorized as tax administrator, tax expert and tax payer. The numbers in each category was equal of twenty. The respondents were asked to tick the answer of their choice or to put the ranking numbers as first choice was the most important and last choice was least important. The responses collected thus were tabulated and analyzed in proper way. The following table shows the groups and number of respondents.

Table 4.10

Group of Respondents and No. from each category

S. No.	Groups of Respondents	No.
1.	Income Tax Experts	20
2.	Income Tax Administrators	20
3.	Income Tax Payers	20
	Total	60

Source: Opinion Survey

4.2.2. Result of Empirical Investigation:

There were 12 questions in the questionnaire to collect opinions from respondents. Result of empirical study has been stated individually in coming paragraphs:

1. Role of income tax in government's revenue

To know what the role of income tax should be in government's revenue, a question was asked "What do you consider the role of income tax in government's revenue?" The responses are tabulated below.

Table 4.11

Role of Income tax in Government's revenue

Responses Respondents	Significant		Moderate		Insignificant		Total	
	No.	%	No.	%	No.	%	No.	%
Tax Administrator	16	80.00	4	20.00	0	0.00	20	100.00
Tax Experts	14	70.00	6	30.00	0	0.00	20	100.00
Tax Payers	11	55.00	8	40.00	1	10.00	20	100.00
Total	41	68.33	18	30.00	1	1.67	60	100.00

Source: Opinion Survey

From the opinion Survey, it was found that 80 percent of tax administrators, 70 percent of tax experts and 55 percent of tax payers think that the role of income tax to be significant. 20 percent of tax administrators, 30 percent of tax experts and 40 percent of tax payers think it to be moderate and only 5 percent of tax payers thinks it to be insignificant. In total 68.33 percent of respondents consider the role of income tax to be significant, 30 percent respondents to be moderate and only 1.67 percent respondent consider the role insignificant. Thus it can be considered the role of income tax to be significant in government's revenue.

2. Contribution of income tax revenue of Nepal

To know respondent's opinion towards current collection of income tax in Nepal a question was asked "What do you think about the contribution of income tax in revenue of Nepal?" The responses are summarized below.

Table 4.12

Contribution of Income Tax Revenue in Nepal

Responses Respondents	Satisfactory		Moderate		Unsatisfactory		Total	
	No.	%	No.	%	No.	%	No.	%
Tax Administrator	7	35.00	12	60.00	1	5.00	20	100
Tax Experts	3	15.00	10	50.00	7	35.00	20	100
Tax Payers	6	30.00	12	60.00	2	10.00	20	100
Total	16	26.67	34	56.66	10	16.67	60	100

Source: Opinion Survey

60 percent of each tax administrators and tax payers thinks the contribution of income tax in revenue of Nepal is moderate 50 percent of tax experts also thinks same. 5 percent of tax administrator, 35 percent of tax experts and 10 percent of tax payers declare this to be unsatisfactory and 35 percent of tax administrators, 15 percent of tax experts and 30 percent of tax payers are satisfied with current contribution of income tax to government's revenue of Nepal. In aggregate 16.67 percent of respondents are unsatisfied and 26.67 percent of respondents are satisfied with current condition. Majority of respondents i.e. 56.66 percent thinks it to be moderate. So it can conclude that the role of income tax in revenue of Nepal is neither so optimistic nor so hopeless. It is in moderate condition.

3. Evaluation of new Income Tax Act

As this study focused on effectiveness of new act, respondents were asked "How do you evaluate the income tax act 2002 with compare to former act for the purpose of effective collection of income tax?"

Table 4.13

Evaluation of New Income Tax Act

Responses Respondents	Better		Same		Worse		Total	
	No.	%	No.	%	No.	%	No.	%
Tax Administrator	17	85.00	3	15.00	0	0.00	20	100
Tax Experts	20	00.00	0	0.00	0	0.00	20	100
Tax Payers	18	90.00	2	10.00	0	0.00	20	100
Total	55	91.67	5	8.33	0	0.00	60	100

Source: Opinion Survey

No any respondent thinks the new act to be worse than former act. 91.67 percent of aggregate respondents evaluate the act better which includes cent percent of tax experts, 90 percent of tax payers and 85 percent of tax administrators, of course a huge population. Only 15 percent of tax administrators and 10 percent of tax payers evaluates the act as same as former act. So it can be said easily the new act to be better than former.

4. Important provisions in new Income Tax Act

Income tax act 1972 was replaced by income tax act 2002 with some new features for timely improvement in income tax system. These new features were presented and asked respondents to pick numbers as per importance to know their opinion. The choices of respondents are summarized and tabulated below:

Table 4.14**Important provisions in new Income Tax Act**

S.N	Provision	Total Points Received				%	Rem
		Tax Administrators	Tax Experts	Tax Payers	Total		
1.	Classification of source of Income	138	147	154	439	20.32	I
2.	Clarity on allowable Expenses	157	136	126	419	19.40	II
3.	Method of assessment	125	130	134	389	18.01	III
4.	Provision of fines and penalties	78	70	56	204	9.44	V
5.	Provision of international taxation	52	63	75	190	8.80	VI
6.	Provision for tax on capital gain and dividend	70	57	49	176	8.15	VII
7.	Provision of resident	71	70	72	213	9.86	IV

Source: Opinion Survey, 2007

From the opinion Survey, it was found that the provision of classification of source of income in new act is most important. Serially other provisions are important as listed below:

1. Classification of source of income
2. Clarity on allowable expenses

3. Method of assessment
4. Provision of resident and nonresident person
5. Provision of fines and penalties
6. Provision of international taxation
7. Provision for tax on capital gain and dividend
8. Authorities and responsibilities of tax administrators and tax payers

Other important provisions not included in questionnaire, identified by respondents were:

9. Tax audit
10. Special provisions for banking and insurance business
11. Special provisions for retirement fund
12. Clarity in exemption, rebate and deductions.

To know the relation between views of tax payers and tax administrators on different provisions of new act, we can test rank correlation coefficient. But the views of tax experts are kept constant.

Hypothesis

There is no significant relationship between the views of tax administrators and tax payers with respect to provisions of new act.

Calculation of Correlation by formula,

$$R_{X1Z} = \frac{6 \sum d^2}{n(n^2 - 1)}$$

$$Pr X6.6745x \frac{1Zr^2}{\sqrt{n}}$$

Let variable x and y denote views of tax administrators and tax payers respectively.

Table 4.15

Correlation Test

S.N.	Provisions	Total points (x)	Rank (R1)	Total points (y)	Rank (R2)	Difference of Rank (R1-R2)	Square of Difference (R1-R2) ²
1.	Classification of source of Income	138	2	154	1	1	1
2.	Clarity on allowable Expanses	157	1	126	3	-2	4
3.	Method of assessment	125	3	134	2	1	1
4.	Provision of fines and Penalties	78	4	56	6	-2	4
5.	Provision of international Taxation	52	7	75	4	3	9
6.	Provision for tax on capital gain and dividend	70	6	49	8	-2	4
7.	Provision of resident and non resident person	71	5	72	5	0	0
8.	Authorities and	29	8	54	7	1	1

	responsibilities of Tax Adm and Tax Payers						
	Total						$d^2 \times 24$

Source: Table 6.5

$$R \times 1 Z \frac{6(24)}{8(8^2 Z1)} \times 0.2857$$

$$Pr \times 0.6745 \times \frac{1 Z (0.2857)^2}{\sqrt{8}} \times 0.219$$

Here, r is greater than Pr. The relation is not significant because to be significant r should be 6 times greater than Pr. So null hypothesis is rejected. That means the opinions of tax administrators and tax payers regarding the important provisions of act is significantly different. But there is some relationship between their views because the value of r is moderate.

5. Reason for Reduction of Income Tax just after New Act

In the above chapter it was known that the trend of income tax just after implementation was reduced significantly for few years. To know the view of respondents on this matter one question was asked "The trend of income tax collection before and after new act is not uniform. Why do you think to be so?" Opinions of respondents are presented below:

Table 4.16

Reason for Reduction of Income Tax after New Act

Responses Respondents	Provision of New act		Effect of Change		Other Reson such as conflit	
	No.	%	No.	%	No.	%
Tax Administrator	5	25.00	14	70.00	1	5.00
Tax Experts	7	35.00	13	65.00	0	0.00

Tax Payers	6	30.00	9	45.00	5	25.00
Total	18	30.00	36	60.00	6	10.00

Surce: Opinion Survey, 2007

60 percent of total respondents have to say that the effect of change is main reason for reduction. Any kind of change may bring this type of situation. 70 percent of tax administrators, 65 percent of tax experts and 45 percent of tax payers were of this opinion. Other 30 percent of respondents think it due to provision of new act while remaining 10 percent argued it to be affected by other reasons such as conflict then.

Some of the respondents have picked priority number, no tick mark in questionnaire. They want to tell that little more all of the reasons are responsible, degree of responsibility may only vary. According to result of opinion survey, effect of change is most responsible. Provision of new act and other reasons such as conflict are following factors respectively. This is the conclusion of this question.

6. Attitude towards Income Tax System

There is more than five decades of introduction of income tax in Nepal. Tax system has been suffered from different paces. The objectives of income tax can be fulfilled or not during this period is a vital question. To know what the respondents thinks about development in income tax system they were asked "How is the income tax system in Nepal in your opinion?" Responses are tabulated below:

Table 4.17

Efficiency of Income Tax System

Responses Respondents	Sound and effective		Satisfactory		Poor		Total	
	No.	%	No.	%	No.	%	No.	%
Tax Administrator	3	15.00	15	75.00	2	10.00	20	100
Tax Experts	0	0.00	13	65.00	7	35.00	20	100
Tax Payers	0	0.00	10	50.00	10	50.00	20	100
Total	3	5.00	38	63.33	19	31.67	60	100

Source: Opinion Survey, 2007

Only 15 percent of tax administrator i.e. 5 percent of total respondents think the income tax system in Nepal to be sound and effective, while more than this i.e. 31.67 percent of total respondents think it to be poor. Majority group i.e. 63.33 percent of aggregate which constitutes 75 percent of tax administrators, 65 percent of tax experts and 50 percent of tax payers are satisfied with income tax system in Nepal. Satisfactory itself means an average condition. In summary, study shows the system is neither so effective nor so poor.

7. View towards Income Tax Administration

Questions are always raised about the entire government administration of Nepal. Tax system is not an exception. To know the respondents' view about the human resource working in tax administration, a question was asked: "How is the income tax administration in Nepal in your opinion?" The result was found as follows:

Table 4.18

Effectiveness of Tax Administration

Responses Respondents	Effective		Satisfactory		Poor		Total	
	No.	%	No.	%	No.	%	No.	%
Tax Administrator	2	10.00	17	85.00	1	5.00	20	100
Tax Experts	0	0.00	10	50.00	10	50.00	20	100
Tax Payers	0	0.00	5	25.00	15	75.00	20	100
Total	2	3.33	32	53.33	26	43.33	60	100

Source: Opinion Survey, 2007

The result is not in favor of current administration. 43.33 percent of respondents think the administration to be poor. It means some of the respondents think administration to be poorer than entire income tax system. Among them, 75 percent of tax payers and 50 percent of tax experts blame administration. Tax administrators themselves are just satisfied with current condition since 85 percent of them choose the answer as satisfactory. Only 10 percent of tax administrators are fully satisfied and thinks the administration is effective. In summary it can be said that the tax administrative system of Nepal is not so effective and needs some kind of treatments.

8. Change Required in Rules and Regulation

The existing act and regulation was replaced by new act and regulation recently. One of the objectives of this study was to analysis the change assessed due to this. To know what the respondents thinks about completeness of rules and regulation after change one question "What change should be made in rules and regulation in your opinion to make income system more effective?" Suggestions made by respondents are tabulate below:

Table 4.19**Degree of Change Required in Rules and Regulation**

Respondents	Responses No Change		Timely general changes in rate, limit		Structural Change in Act regulation		Total	
	No.	%	No.	%	No.	%	No.	%
Tax Administrator	1	5.00	17	85.00	2	10.00	20	100
Tax Experts	0	0.00	3	15.00	17	85.00	20	100
Tax Payers	0	0.00	9	45.00	11	55.00	20	100
Total	1	1.67	29	48.33	30	50.00	60	100

Source: Opinion Survey, 2007

This was the question which shows the vast contradiction between the view of tax administrators and tax experts. Rules and regulations require change or not is not the question of doubt because only 1.67 percent of total respondents think no change is required. Degree of change is the main subject of matter. 85 percent of tax administrators are in side of general change while same numbers of tax experts want the large scale change i.e. structural change in rules and regulation. Tax payers are divided into these two groups about equally. So it is difficult to conclude and recommend the degree of change required in existing rules and regulations.

9. Way of improving effectiveness of tax administration system:

For the supplementation of question no 7, if improvement is required in tax administration of Nepal, what should be the degree of change was asked to respondents as "How can be improved the effectiveness of tax administration system?" The respondent response differently as shown in the table:

Table 4.20

Degree of Change Required in Tax Administration

Respondents	No Change		General imp. delegation		Evolutionary change		Total	
	No	%	No.	%	No.	%	No.	%
Tax Adm	2	10	16	80.00	2	10.00	20	100
Tax Experts	0	0.0	8	40.00	12	60.00	20	100
Tax Payers	0	0.0	6	30.00	14	70.00	20	100
Total	2	3.33	30	50.00	28	46.67	60	100

Source: Opinion Survey, 2007

It is already identified that administrative system is not as effective as it requires. 50 percent of total population, which includes remarkable representation of tax administrators, i.e. 85 percent of them thinks general improvement such as decentralization and delegation will solve the problem. But 60 percent of tax experts and 70 percent of tax payers including 10 percent of tax administrators feels evolutionary change is lacking for betterment of income tax administration.

10. Right treatment to administrative staffs to make them more responsible and

energetic:

Tax administration itself is a system, while organization of administrative staffs is most important part. Without changing attitude and perception of human resource working there, it is impossible to think about any kind of change. If tax system or administration requires change, obviously its initiation is to be taken by human resource. To know the respondents' view administrative staffs are lacking incentives or they need penalties and punishments to make them more responsible and energetic or current condition is satisfactory, question was kept that "How tax administrative staffs can be made more responsible and energetic?" In contest of our country where government staffs are always criticized for their performance and behavior, what the respondents' answer, let's look at following table:

Table 4.21

Treatment to administrative staffs to make them more responsible and energetic

Respondents	Providing different incentives and trainings		Tight rules and regulation in service		Nothing is required		Total	
	No.	Percentage	No.	Percentage	No.	Percentage	No.	Percentage
Tax Adm	17	85.00	3	15.00	0	0.00	20	100
Tax Experts	11	55.00	9	45.00	0	0.00	20	100

Tax Payers	8	40.00	12	60.00	0	0.00	20	100
Total	36	60.00	24	40.00	0	0.00	60	100

Source: Opinion Survey, 2007

Nobody is satisfied with current performance of administrative staffs, since no one thinks nothing is required. Obviously 85 percent of tax administrators want different incentives and trainings to improve performance of staffs which is usual. 55 percent of tax experts and 40 percent of tax payers support them. In the other hand 60 percent of tax payers demand tight rules and regulation in service to bind them and get support from 45 percent of tax experts and 15 percent of tax administrators. There is no exact choice since views of respondents have divided into 60:40 ratios. So it can be said that both kind of treatment is essential, incentives are to be provided firstly and if performance already not found to be satisfactory, provisions of penalties should be introduced.

11. Way to make taxpayers more responsible

Responsible taxpayers are the most important factor of effective and sound tax system. Our tax system cannot be exception. Whether the question is raised about tax system, we must look at different factors related to taxpayers. These factors may be degree of awareness, feelings of responsibilities, attitude of taxpayers, economical environment etc. If our tax system is seems to be not efficient, we must consider the side of taxpayers. To know how the respondents think to improve attitude of taxpayers, question was asked "What is the most suitable way to make taxpayers more responsible?" Suggestions made by respondents are tabulated below:

Table 4.22

Way to make taxpayers more responsible

Responses	Awareness through media		Harder provisions in rules		Incentives such as prize and respect		Nothing is required		Total	
	No.	%	No.	%	No.	%	No.	%	No.	%
Tax Administrator	9	45.00	5	25.00	6	30.00	0	0	20	100
Tax Experts	7	35.00	6	30.00	7	35.00	0	0	20	100
Tax Payers	8	40.00	2	10.00	10	50.00	0	0	20	100
Total	24	40.00	13	21.67	23	38.33	0	0	60	100

Source: Opinion Survey, 2007

From the opinion Survey, it was found that 45 percent tax administrator, 35 percent tax expert and 40 percent of tax payers think tax payers not to be aware. So they recommend for awareness through different media. 21.67 percent of respondents have opinion that tax payers are aware but have intension to evasion so it requires harder provisions in rules. Fines, penalties, punishments etc. can bring them in track. Other 38.33 percent respondents including 50 percent of tax payers, 35 percent of tax expert and 30 percent of tax administrators identify the tax payers as responsible citizens and argued incentives such as prize and respect will motivate them. According to survey result, all provisions are to be implemented simultaneously.

4.3 Major Finding of This Study

Major findings of this study through different analysis are summarized below:

1. Government revenue is not sufficient to cover the growing expenditure in Nepal so resource gap is widening. Resource gap of 50445.5 million in FY 2001/02 reached to 82135.30 million in 2006/07. It is continuously increasing rapidly.

2. The basic sources of revenue are tax revenue and non tax revenue but collection of these revenues is not sufficient to cover expenditure in Nepal. The tax revenue has very dominating role i.e. 75.74 percent of total revenue in 2002/03 and 77.36 percent in 2006/07. Share of non tax revenue for the same period seems to be 24.26 percent and 22.63 percent respectively. The tax revenue contributed amount of 42587 million and 63542.20 million in 2002/03 and in 2006/07 respectively.
3. The tax revenue constitutes direct and indirect tax. Within indirect tax the VAT and costume are in first and second position by their share in total indirect tax in recent years. Indirect tax has a leading role in total tax revenue. Its share was 76.27 percent in FY 2002/03 and reduced to 76.97 percent in 2001/02 and gradually increased to 76.44 percent in 2006/07.
4. Income tax is the major source of direct tax revenue. The amount from income tax was 7966.2 million in 2002/03 and was 11373.7 million in 2006/07. Income tax constitutes Income tax from public enterprises, semi public enterprises, private. Corporate bodies, individual, remuneration and tax on interest.
5. The role of income tax from public enterprises is significant. It has contributed 21.2 percent to total income tax in average. The share of income tax from private corporate bodies is 19.5 percent in average.
6. Income tax from individual has the major role in income tax and bears dominating role in period of the study. It has contributed up to 42.20 percent in 2002/03. Its lowest share is 38.20 percent in 2003/04 and average share is 42.5 percent.
7. Income tax from public enterprises has mostly effected. Its contribution was 2056.60 million in 2003/04 and is unable to meet the record again.

It declined to 1332.40 and 195.7 for first two years of new act. It has positive symptom in 2003/04 when growth of 64 percent occurs but after this, its condition is poor. For year 2006/07 its decline rate is 85.3 percent.

8. The effect in income tax collection from private corporate bodies is declined for first two years of new act, slow growth for third year and rapid growth for last two years. The effects of act seem to be very positive as its contribution to total income tax has risen to 32.8 percent for FY 2005/06.
9. It was not due to other reasons because other economic activities did not show this type of fluctuating situation. Comparison of income tax with other economic factors such as GDP, total revenue, total tax revenue and total direct tax revenue shows the facts, which were also fluctuating.
10. Corporate tax contribution on government revenue is less contribution in other source. In our country corporate sector is very huge but contribution of revenue is less because of the tax avoid and erosion.
11. Government of Nepal is not follow the properly his rule and regulation where the government is unstable. That is why it is not satisfactory in the corporate sector contribution of government revenue.

An empirical study was conducted during the study to know the views of different sector of income tax about role of income tax, features of new act, condition of income tax system and administration in Nepal and suggestion for betterment of income tax system in Nepal. Major findings identified from empirical study are as follows:

1. Role of income tax should be significant in government's revenue.

2. Contribution of income tax in revenue of Nepal is neither so optimistic nor so hopeless. It is in moderate condition.
3. Income tax act 2002 has better provisions than former act.
4. Classification of source of income, clarity on allowable expenses, method of Assessment, provision of resident and nonresident person etc are the major important factors of new act. Tax administrators and tax payers have not same view towards importance of factors.
5. Effect of change is most responsible for not uniform contribution of income tax before and after enactment of new act. Provision of new act and other reasons such as conflict are following factors respectively.
6. Income tax system in Nepal is neither so effective nor so poor. It is just satisfactory which means average condition.
7. Tax administrative system of Nepal is not effective and needs some kind of treatments

CHAPTER - V

5. SUMMARY, CONCLUSIONS AND RECOMMENDATIONS

5.1 Summary

The role of government is increasing as concept of welfare state is introducing. It requires fund to improve lifestyle of people, lunch public welfare program and maintain law and order. Fund is collected by government through external and internal sources. External sources such as foreign loan, grants, borrowing etc is not certain and not good for sustainable economic development of country so any government has to emphasis on internal sources such as tax and non tax revenue to collect necessary fund.

Nepal is one of the least developed countries of the world. Besides it is trying on planned development over five decades, already suffering from resource constraints, massive poverty, rapid growth of population, increasing frictional and seasonal unemployment, diseases, aggressive dependent on the agriculture, subsistence living standards and poor infrastructure. To overcome such serious problems government requires lots of fund but resource mobilization is still poor in Nepal. The resource gap i.e. the gap between government expenditure and internal source is widening continuously. There is no alternative to mobilize internal resources and collect funds internally through revenue for rapid and sustainable economic growth.

Revenue constitutes tax and non tax revenue. Direct tax and indirect tax are branches of tax revenue and income tax is one of the major sources of direct tax. Income tax is imposed on net income of natural as well as legal person. It is called personal income tax if levied from natural person and called corporate income tax if levied from any corporation.

History of income tax starts from eighteenth century in world, initiated from Britain. In Nepal systematic provisions of income tax was introduced in 1959 through economical act. Business Profits and Remuneration Act 1960 and Nepal Income Tax Act 1962 made the provisions more systematic and effective. Income Tax Act 1974 was introduced after long consultations and homework according to economic policy of nation then. Different amendments were made in the act for timely corrections. To make timely improvement in Nepalese tax system according to modern economy and tax system of other countries and facilitate the system with concept of world trade, globalization, economic liberalization etc, Income Tax Act 2002 was passed through legislation and carried in practice.

This act has broadly divided the income into three categories: Employment income, Business income and Investment income. It has some new features such as concept of capital gain, pool system of depreciation, resident and nonresident person, international taxation etc and has made timely improvement in some other provisions.

5.2. Conclusion

Internal revenue collection is the most reliable alternative to bare expenditure of government and conduct development activities. Income Tax is one of the important and relevant sources of revenue since it follows the basic principles of taxation such as equity and progressively.

State makes policies, rules and administration as per need of entire country to collect revenue through tax and non tax sources. Nepal has made change in income tax act in 2002 as per need. The change has shown some effects on collection of income tax. It has broken the trend then and has got a new trend after the year. Although there are some difficulties in language, discretionary powers etc, different provisions in new act are as per need of time and

economic environment. Well implementation of this act will guide Nepalese income tax system to hopeful direction. Income tax system in Nepal is not fully satisfactory. Due to economic liberalization and globalization, very important source of revenue i. e. custom duty is not in condition to bare its current share in coming days. So importance of internal sources such as income tax will increase in coming days. But there are many problems in Nepalese income tax system. Inefficient tax administrative system, widespread income tax evasion, complicated and frequent change in tax rate and lack of awareness and feelings of responsibility in taxpayers are appearing as major factors for low contribution of income tax in national revenue. Internal conflict of nation and political instability has affected the economic system indirectly but very seriously. It has damaged as well as destroyed the environment for generating more income. Where income is limited, certainly the tax from income will not be so optimistic. In changing scenario, it seems to be necessary to give sufficient attention towards income tax system by all concerned parties for rapid and sustainable economic development of country.

The conclusion tax avoidance is the reduction of that liability through the manipulation of existing law. It is legally permissible but unethical. Section 35 of the income tax act define tax avoidance as any means or arrangement one of the main purpose of which is the avoidance or reduction of tax liability. This act made the provision against tax avoidance. This act has given certain rights to IRD to minimize tax avoidance. As per the act, the Department can re-characterize an arrangement or part of an arrangement that is entered into or carried out as part of a tax avoidance scheme. It can also disregard an arrangement or part of an arrangement that does not have substantial economic effect and re characterize an arrangement or part of an arrangement that does not reflect any substance. The other provisions kept in this act to reduce tax avoidance are;

- a) Use of arm's length price to avoid transfer pricing.
- b) Provision against splitting of income.
- c) Provision of not allowing reducing dividend income.
- d) Provision of not allowing double expenses under lease sale
- e) Right of tax authority to have access to the information of tax payers.

5.3. Recommendation

The following suggestions are made for betterment of income tax system in Nepal.

1. Overall revenue policy as well as tax policy should be revised through detail and critical analysis of situation.
2. Before making any kind of change in policy, rules and regulation, whole system is to be prepared to accept it.
3. All stakeholders are to be aware about the change in detail.
4. Organizational system to be established for broadens tax net. Special provisions for tax evaders and persons conducting business without registration should be introduced.
5. Provisions of act and regulations are to be improved or changed as per need. Following factors are to be considered while making change:
 - a. The language should be clear and simple.
 - b. Rules and regulations should not be changed for just change. It should fulfill the need of situation and time and should be based on ground of reality.

- c. Provisions of fines and penalty amount and rate are to be revised each year.
 - d. Discretionary power of the tax officials should be curtailed by act.
6. Administration is the tool to implement all policies and rules. So, effectiveness of income tax system depends upon the income tax administration. It is clear that the effectiveness is lacking. Suggestions for improvement of income tax administration are as follows:
- a. Administrative staffs should be well trained about system.
 - b. Monetary and non monetary incentives are to be provided to administrative staffs as per need to motivation and to improve their performance.
 - c. Provisions of penalty and punishment should be realistic and logical. It should be well implemented for them who do not fulfill their responsibilities and expects unlawful returns.
7. Tax payers are the most important factor of tax system. Suggestions regarding tax payers are as follows:
- a. Awareness and brain storming of tax payers should be emphasized. Workshops and media should be used to educate taxpayers and improve their attitude.
 - b. Regular and effective reward system should be started for responsible taxpayers to encourage paying tax voluntarily.
 - c. Harder provisions of fines, penalties and punishment should be well implemented to intentional tax evaders.

8. Tax offices should be decentralized for broad coverage of geographical region. Separate income tax department should be established for specialization of income tax.
9. Different recent technologies such as e-taxation should be introduced and promoted to avoid complexities and delay in income tax administrations. Tax audit system should be timely improved and equipped to work with modern technologies of account keeping.

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