CHAPTER -1

INTRODUCTION

1.1 Background of the Study

Economic development is the prime concern for each nation of the world. For the economic development, government bears huge responsibility towards its people. To fulfill its responsibility, government needed revenue to operate different activities in a country. Such activities include general activities and developing activities. General activities are made for the protection of common people and public administration. Development activities are made for providing transportation, education, health and public utilities facilities to the community. Government collects revenue through two sources: (i) internal & (ii) external.

Being a developing country, Nepal has limited sources of internal funds so most of the development activities depends on the external sources. The external financial source comes under the head, bilateral & multilateral grants, loans from foreign countries and fund from donor agencies. These sources are equipped with some of the conditional factors as limited, inconvenient and not suitable to boost up the Nepalese economy due to the vested interest of the programs and policies of the donor countries & agencies and need to pay high interest accepting the inappropriate condition to take the loan. Government tries to finance resources through internal sources. It is very important for a country like Nepal to make effective use of internal resources where adequate natural resources and low cost labor-force are available. Till date Nepal is not able to utilize its natural resources effectively, because of various reasons as, the small and stagnant industrial sector, partial monetization of the economy, poor performance of public sector enterprises, poor rate of economic growth, inadequate tax efforts, deficiencies on tax policies, laws and administration etc.

Internal sources of public funds are important not only for necessary financing of funds, but also for proper utilization of external sources. Based on the nature of sources, public funds are classified as revenue (public income) and borrowing (could be external and internal). The public income or revenue includes: (a) taxes (b) revenue from Government corporations and public enterprises (c) fees (d) special assessment (e) fines and penalties. Among them tax is the main sources of collecting the government revenues. In Nepal, about 77% of total revenues come from tax revenues and the rest 23% from non-tax revenue (Amatya, pokheral and Dahal, 2004: page 3).

According to Seligman (as cited in Kandel 2005) "A tax is a compulsory contribution from the person to the government to defray the expenses incurred in the common interest of all without references to special benefit conformed." Kandel again, cited that the tax is levy paid or to be paid by the natural or an artificial person to the government without getting corresponding benefits of goods or services provided by government. Thus, taxes play vital role in the government revenue.

Simply, tax is a compulsory contribution to the state from a person. The natural person or artificial person (entity or corporate body having tax liabilities) pays taxes to the government. The taxpayer does not receive the equivalent benefit from the government. Tax is paid to government which is further expensed by the government for common benefits and interest of the people.

As per the charge on concerned person, Taxes are classified into two major categories viz, direct tax and indirect tax. The tax directly paid by a person on whom it is legally imposed is known as a direct tax. Such as income tax, gift tax, interest tax, property tax, vehicle tax, house & Land tax, contract tax etc. Whereas, a tax that is imposed to one person but partly or wholly paid by another is termed as indirect tax. Such tax may be custom duty, value added tax, entertainment tax, excise duty, sales tax, hotel tax, passenger tax etc. In Nepal, direct tax contributes about 21% and Indirect tax contributes about 79% in the tax revenue of government (Amatya, Pokharel and Dahal 2004: page 3,4).

Income tax is one of the most popular direct tax. It is charged on person's income according to the law of nation. Income includes all the income, received from business, investment & employment. Income tax is superior to indirect tax because it is imposed on the basis of paying capacity of the taxpayer. People whose income is below the taxable income are free from the obligation to pay tax. It may be possible to reduce the gaps in income by imposing higher rate to those who are having high income and from that collected amount, providing necessary to the people with very poor economic condition. Hence, it will help for the people with very poor economic condition. It may help to make equitable economic distribution in the society. Balanced regional economic development is also possible through the provision of income tax. The government should charge higher income tax on the income from urban area and less on the income from remote area. Income tax holiday and incentives would help to develop the priority sector of a national economy. "Income tax has become an effective investment to ensure balanced socio-economic growth" (Mathew (1975), Musgrave & Musgrave (1998).

Income tax plays an important role in the Nepalese economy. It is the major source of government revenue. It is recognized as a good financial tool to narrow inequality of income. It helps to reduce regional economic imbalance by providing tax concession and holiday to business or industry, which are established in remote area. It is also helpful for generating the concept of social responsibility towards the nation and keeps the people vigilant to see the public money not to be misused.

The contribution of income based tax is much smaller to the total revenue for developing countries in comparison to developed countries and is likely to remain same for some time to come, despite the efforts over the years of many by least developed countries to raise more revenue. There are mainly four reasonswhy income tax yield is less in developing countries as compared to developed ones. They are problems of defining income, problems of assessing and measuring it, the choice of rates, allowance & deduction and difficulties of tax collection.

Income tax itself being main source of government revenue, is a tool to balance economic development. No one can doubt that, the equal distribution of income is possible by the implementation progressive income tax. Now, it is realized that contribution of income tax to the revenue of government should increase in Nepal. Nepal has adopted the income tax system for last four & half decades. But Nepal's past experience shows that the government is unable to maximize the share of income tax to the public fund as per expectation. Being developing country, Nepal is facing many problems in financial sectors. Merchant Bankers plays a vital role in economic and financial development of the country acting as a bridge, which provides all kind of financial assistances to industries and commerce. It plays significant role in mobilizing funds of savers to ingestible channels assuring of promising return on investments and thus can help in meeting the widening demand for ingestible funds for economic activity. The service of merchant banker could cover project counseling and pre-investment activities, feasibility studies, project reports, design of capital stricture, issue management and underwriting, loan syndication, foreign currency finance, merger, amalgamations and takeover, venture capital and public deposits.

As per Securities Act, 2007, any institution having license from securities board to act as merchant banker is authorized to perform merchant banking activities.

Merchant Banking Regulation, 2064, classifies merchant banking activities as issue and sales management, securities underwriting, share registration and investment management. Paid up capital of the institution is determinant for the different types of merchant banking activities to be performed.

Table 1.1 Paid Up Capital versus Merchant Banking Activities

S.N.	Merchant Banking Activities	Paid Up Capital (Rs. In '000)
1	Issue Manager	3,00,00
2	Underwriter	4,00,00
3	Share Registrar	1,00,00
4	Investment Management	1,00,00
5	All activities as mentioned above	7,00,00

Here lots of financial systems are being slowed down due to insufficient capital, technical and financial support. Merchant Bankers encourages them by its versatile service like project counseling, corporate counseling, portfolio management and venture capital and issue management.

Table 1.2 Name list of Merchant Bankers licensed from Securities Board of Nepal

S.N.	Names	Address
1	Ace Development Bank Ltd.	Narayanchour, Kathmandu
2	NMB Bank ltd.	Babarmahal, Kathmandu
3	Citizens Investment Trust	Putalisadaki, Kathmandu
4	NIDC Capital Markets Ltd.	Kamalpokhari, Kathmandu
5	Nepal Finance Co.Ltd.	Kamaladi,Kathmandu
6	Nepal Share Markets and Finance Ltd.	Ramshahapath, Kathmandu
7	United Finance Ltd.	Kamaladi, Kathmandu
8	National Finance Co.Ltd.	Pako Newroad, Kathmandu
9	Elite Capital Ltd.	Jamal, Kathmandu
10	Vibor Development Bank Ltd.	Tripureshwor, Kathmandu
11	Nepal Housing & Merchant Finance Limited	Dillibazar, Kathmandu
12	Development Credit Bank Ltd.	Kamaladi, Kathmandu

However this study contains only that of seven Merchant Bankers as follows,

- Nepal Finance Company Ltd.
- NMB Bank Ltd.
- Citizens Investment Trust.
- Nepal Housing & Merchant Finance Ltd.
- Development Credit Bank Ltd..
- NIDC Capital Markets Ltd.
- Nepal Share Markets and Finance Ltd.

A good merchant banker would be considered as that, one who is expert, honest, have integrity and capacity to develop public relation. Whenever a business concern needs funds from the capital market it would usually approach the merchant banker rather than banks or financial institutions. By providing various services to public, business organization and government, merchant banker earns profit & pays income tax out of their net profits. It therefore plays a contributory role in government revenue and national economy of a country.

1.2 Statement of problem

Underdeveloped countries are facing various problems in the process of economic development. For the economic development sufficient resources is needed. One of the major sources of the public revenue is income tax which is charged on person’s income. For the proper management of national operation and development, governments expenditure should match with the income, so increase in expenditure results governments to search for alternatives to increase its income. But the expenditure of government of Nepal is being increased in a faster rate than the increment in revenue. Being developing country, most of Nepalese people are below the poverty line nearly one third of the total population (about 31.8%) live below poverty line as per the Nepal Standards Survey 2003/04) and GDP per capita is $ 383 (According to MOF Report 2006/07). It shows that it needs huge amount of capital for economic development of Nepal. It is possible only when the volume of resource could be match with the requirement.

Nepal itself being developing country, like other developing countries of the world should make heavy investment on infrastructure, social activities and economic development of the nation. That's why, the government is always in pressure to spend huge amount in education, health, physical construction and so many areas. There seem to be three reasons contributing to strong pressure to spend (Leaving aside general price changes): the growth of population; the emergence of strong local and the emergence of strong world options.

The development of the country will be possible when the government can mobilize its own internal revenue, which constitutes tax and non-tax revenue. Tax revenue constitutes a significant position in government revenue. In the total tax revenue indirect tax has greater portion than direct tax. In Nepal only 0.5% of the total population pays the income tax (Economic Survey 2005/06). Past experience shows that, there is poor tax paying habit in Nepalese people. There are various problems associated with income tax administration like, improper record about the number of income tax payers, defective selection of personal, lack of training and education to tax payers and tax officers, undue delay in making assessment, lack of responsibilities of officials on their work, existence of corruption, and lack of motivation to concerned authorities etc. Because of the inefficiency of the administration and increasing corruption, people have no faith in the working of government and its organization.

The income tax is the vital source of the government revenue. According to the nature of Tax payer income tax is categorized as personal income tax and corporate income tax. Most of the personal taxpayers do not reveal the income source even though they earn significant amount. They hardly keep their accounts. Similarly, some companies are practicing to evade the tax liabilities by hiding incomes. As a result, the actual collection of income tax is very low and problem has been stable continuously due to corruption too. The laws of tax authorities also cause low revenue generation to the government. The discretionary power of the tax personal and the tax assessment procedure of the income tax system of Nepal harass the taxpayer in the payment of tax results in the reduction of the income tax revenue. Similarly the department cannot locate its taxpayers plus the actual number of income tax payers.

In the context of being in developing phase, development countries like Nepal, government cannot raise more income tax from corporate sector because high income tax may discourage the investment in corporate sector. Government of Nepal, being unable to realize the expected income tax from personal as well as corporate sector are, no proper supervision over the staff member of tax collection department, and corruption. There is no reliable and sufficient data for tax purpose.

However Merchant Bankers assist government to collect its revenue though making profit from the financial transaction by rendering service to the public and business organization and pay income tax from their taxable income.

1.3 Objectives of the Study

The main objective of the study is to analyze the income (corporate) tax collection from Merchant Bankers by the government for the last five years. The other major objectives of this study are listed below.

1. To analyze the role of income tax in National Economy of Nepal.
2. To introduce merchant bankers service in Nepal and evaluate the contribution of income tax paid by selected merchant bankers to the government revenue.
3. To assess the contribution of income tax paid by selected Merchant Bankers on total income tax and total tax revenue of the government.

4. To forward the appropriate suggestions and recommendations for the identified issues.

1.4 Significance of the Study

For the economic development of the nation there is necessity of huge outlay amount. But resources available for investments are limited. Government should identify the potential taxpayer and should give more emphasis to collect more revenue from them. For the economic development of the country, contribution of direct tax is more essential than indirect tax. But in contrast to such the whole tax structure of Nepal is dominated by indirect tax. Among the direct tax, income tax plays a significant role. It is one of the major resources which can be increased through proper correction in collection procedures and identification of potential taxpayers. So, it becomes necessary to analyze the different taxpayers under each head and income tax collected from each group of taxpayers time to time.

To increase the portion of national revenue, research and analysis should be done in the field of income tax. But in contrast to such, the studies and research work is lacking in the area of income tax. Merchant Bankers are also income taxpayers. The problems they are facing in tax paying should be corrected so they may contribute more income tax as the national receipt. Merchant Bankers are such institutions, which are directly linked with most other business activities. The position of business, trade and industries can be visualized through the analysis of activities of Merchant Bankers. This study concern with appropriate suggestions for the estimation, correction and provide comprehensive information about income tax. Besides, this analysis may be useful to make new policies for granting various facilities to the Merchant Bankers for making more taxable income in the competitive environment and legal correction, vague section of income tax can also be rectified from such analytical study.

This study is concerned with these aspects and tries to make appropriate recommendation for the correction of problems in paying income tax by Merchant Bankers. Beside this, study will also be useful to the tax planner, bankers, tax authorities and many others like teachers, students, researchers, and people who are interested on it.

1.5 Limitation of the study

As every research study is followed by some limitations, this study is also not free from limitation. The Major limitations are mentioned below:

1. The study is concerned only on some of the sample merchant bankers selected from the whole population.
2. This study concentrates on the income (Corporate) tax realization from selected seven Merchant Bankers. They are;
   - (I) Nepal Finance Company Ltd.
   - (II) NMB Bank Ltd.
   - (III) Citizens Investment Trust
   - (IV) Development Credit Bank Ltd.
   - (V) NIDC Capital Markets Ltd.
   - (VI) Nepal Share Markets and Finance Ltd.
   - (VII) Nepal Housing and Merchant Finance Ltd.
3. The study has covered the data from fiscal year 2002/2003 to 2006/2007
4. Mainly secondary data has been used.

1.6 Design of the study

The Study has been divided into major five chapters. They are as follows:

Introduction: The first chapter covers introduction, background of the study, statement of the problem, objective of the study, significance of the study, limitation of the study and design of the study.

Review of Literature: The second chapter focuses on review of literature. It is related survey of books, journals, thesis & dissertation and articles.

Research Methodology: The third chapter deals with research methodology to be adopted for study consisting introduction, research design, population and sample, nature and sources of data, data collection procedures, research variable and tools and technique employed.

Data Presentation and Analysis: The fourth chapter has deal with the presentation & analysis of data collected with figure and picture.

Summary, conclusion and recommendation: The fifth chapter deals with findings, conclusion, recommendation and suggestion.

CHAPTER – II

REVIEW OF LITERATURE

Government expenditure is increasing day by day because of demand of time, increase in population, social progress, increase in price, security etc. To meet the growing public expenditure, the government has to manage its fund. It is received from different sources. To fulfillment the responsibility, the government collects revenue from public enterprises, specially assessment, fees, fines and assistance etc. Among them tax is main source of government revenue. Simply, tax is a liability to pay an amount to the government. It is a compulsory contribution to the national revenue from the tax payers according to law.

According to Prof. Seligman "A compulsory pay from a person to the government to defray the expenses incurred in the common interest of all without reference to special benefits concerned".

According to Plehn "Taxes are general contribution of wealth levied upon persons, natural or corporate to defray expenses incurred in conferring common benefits upon the residents of the states".

These definitions of tax clearly points out that;

- Tax is a compulsory levy and taxpayers should not expect of particular return of goods or services by the government.
- Tax is a liability imposed upon the tax assesses who may be an individual, groups of individuals, or other legal entities.
- Tax amount is spent for common interest of people.
- Tax is imposed as per government rules and regulation.

- Tax is a major head of internal revenue for government; the government utilizes the collected taxes for peace, security, day to day administration, economic development program, and health and so on.

Taxes are broadly divided in to two categories:

1) Direct tax
2) Indirect tax

Direct tax: If a person directly pays the tax liability to the government it is known as direct tax. It includes income tax, gift tax, interest tax, property tax, vehicle tax, house and land tax, expenditure tax, death tax and contract tax. The direct taxes have been used to bridge the gap of income and wealth inequality in the society.

Indirect tax: It is levied on the person who does not bear it from her/his own income. Indirect taxes are imposed on the consumption of goods and services. It includes expert/import duty, excise duty, sales tax; value added tax, entertainment tax, hotel tax, passenger tax etc.

Taxation is a major instrument of social and economic policy.

- It reduces inequality of economic development by reallocation of resources.
- It transfers resources from the private to public sector.
- It is also useful for resource mobilization through capital formation.
- It promotes economic growth, stability and efficiency.

Concept of Income Tax

After the great depression of 1930's the function of government increased considerably. Government goes towards various sources for the collection of government revenue. Among various sources of revenue, tax is founded as a major source. Generally tax is defined as compulsory payment to the government. Everybody, on whom tax is imposed, should pay tax.

Income tax is imposed on net income of individual and corporation. Tax assignee must bear the burden of tax imposed on them. Generally, income means the inflow of cash to the person. Income tax is levied on the income derived from business, employment and investment. Income tax is levied on the net income i.e. Total income less the allowable deduction. It is a best measure of economic well being of a person as well as of nation. Higher income denotes the high living standard and lower income refers to the low living standards of people.

Economists defines the term 'income' in a broader sense as, an economic gain or receipt to a person during a particular period by way of wages, interest, profits and rent. The money income of the people could be utilized for two purposes for consumption and saving. This definition can be expressed in the formula as below;

$Y = C + S$

Where,

Y = Income

C = Consumption

S = Saving

According to income tax Act 1974 (2031) "Income means the income earned or received in cash or kind from the sources as besides employment and investment." In Income Tax Act, 1974 (2031) there were five heads of income tax. They were:

(i) Agriculture, (ii) Industry, Business, Profession or Vocation, (iii) Remuneration, (iv) House and Land Rent and (v) Other Sources.

The new income tax Act, 2002 (2058) was passed and implemented from 2058 Chaitra 19 (1^{st} April 2002). This act defines the term income as, income of any person derived from employment, business, investment and accumulated income calculated as per the act. This act classifies the income into three different heads they are: (i) Business, (ii) Employment and (iii) Investment.

Tax means income tax to be paid or would be payable according to Income Tax Act or prevalent law of Nepal. According to this definition, tax includes fees, additional fees, deposits and fines. The constitution of kingdom of Nepal 2047, has prescribed that "No tax shall be levied and collected except in according with law". Therefore, only taxable income as calculated by the prevalent rule is subject to tax so that the objective and principal of taxation will be fulfilled. (Income, Tax Act 2002 (2058)

Income tax refers to the tax levied on the income of a person and profit of the corporate sector for the specified time period particularly one year. In a board sense, income tax is a levy based upon the production, receipts or gain of the taxpayer within a definite period of time.

2.2 Evolution of taxation

The Great Britain is the first country in the world to introduce income tax in 1799. It imposed income tax in order to finance war with France. Similarly, in USA the first federal income tax was imposed in 1862 with the same objective (to finance civil war). However, in the beginning, these countries imposed income tax as temporary until 1860. There after, since 1913 it was accepted as permanent tax. Thus, income tax was adopted by different countries gradually. Italy started it in

1864, and New Zealand adopted in 1891, Austria and Canada had followed the income tax in 1915 and 1917 respectively. After First World War the income tax became an important source of government's revenue in many developed countries. By 1939, it became the most important source of revenue in most developed countries and made appearance in a number of developing nations. (Agrawal, 1980)

In India the income taxation was started in 1860 by the British government to have relief from economic burden created due to first democratic revolution. It was then regularly collected after the publication of Income Tax Act 1886. (Dhakal, 2057)

In this way, income tax has become the regular source of national receipts for many developed and developing countries of the world. In the beginning, income tax was generally levied at a flat rate. The principal of progressive rate of income tax had been adopted by the United Kingdom and New Zealand since 1909. Now days the progressive rate is commonly used rather than flat rate in all over the world.

2.3 Evolution of Income Tax in Nepal

In the time of king Amsuvarma, there was existence of irrigation tax and religious monuments preservation tax. There exist tax for purification of castes by priests and even cremation tax, which was extracted in gold by then ruler of Bajhang in far western Nepal. In the ancient Nepal, the taxes were levied in the form of cash, kind and labor. In the regime of study of Lichhvi period also the main source of government revenue was taxes. These were very much specific in nature. The taxes were known as “Bhaga”, “Bhoga” and “Kara”. The Bhaga tax was levied on agriculture, kara was levied on business and Bhoga was tax levied on animals.

During the period 1768-1816 (unified Nepal), the main sources of Nepalese revenue were land and homestead taxes, monopolies customs, transit and market duties, mines, the export of forest produce, birds animals and various levies and fines. The taxes were usually collected at three levels.

1) Royal palace - to finance occasional and ceremonial needs.

2) Government - to finance administrative, military and other purposes, assessed of official.

3) Local - perquisites of local official, functionaries and mendicants.

During the 104 years rule (1847-1951) of Rana family in Nepal the taxation was imposed to fulfill the objectives, needs and whims of the then ruling Prime Minister. At that time, the source of revenue were land tax, customs and excise duties in the form of lump sum contracts, royalties on felling of trees, royalty on supply of porters and soldiers, entertainment tax and a few other minor taxes. In modern Nepal after the downfall of Rana regime, various types of direct and indirect taxes had been brought in use in order to finance the growing development expenditure.

2.3.1 Taxation in Ancient in Nepal

Tax has been one of the major sources of national receipts since the ancient time in Nepal. In those days tax was collected in the form of cash, kind and labour from the merchants, travelers and farmers. However, the nature of tax levied by the government was temporary type in the old age. In the Lichhvi regime (known as Golden Era), taxes were the main source of revenue. During that period, taxes were known as Trikar, which meant three kinds of taxes viz. Bhaga, Bhoga, and Kara. The Bhaga tax was levied on agriculture, Boga was on animal and Kara tax was business income. Apart from direct taxes, for the first time in the regime of King Ansubarma in Nepal, irrigation tax and religious monuments preservation taxes also existed. The farmers had to pay tax on income from agriculture to the government in 1/6, 1/8 and 1/12 shares of production depending on the quality of the land possessed by them. All artists had to donate labor compulsorily as the tax payment. (Adhikari, 2059).

2.3.2 Taxation in Unified Nepal (1768-1846)

After unification of the Kingdom of Nepal, expenses for administration, military and other operational activities increased gradually. During that period, the taxation had been taken as main source of revenue and different types of taxes like land tax, transit tax, market duties, forest product tax and mining tax were levied. The main objective of imposing those taxes was to maximize the national revenue. In that period taxes were collected from three levels: Royal palace, Central government and Local authorities. They collected cash or goods from taxpayers as tax. Royal palace levied taxes like Walak, Gaddimubarak, Chumawan and Goddhawa. Government levied taxes like Darshan Bhet and Salami and local authorities levied taxes on forest and water sources; commercial taxes like customs; transits and market duties; mines and mints; export of forest product like herbs, wax drugs wild life, birds, elephant and judicial fines. Taxes from land and business were type of direct tax among the all taxes during that period. (Dhakal, 2001)

Walak was from each family in the period of national celebration or festivals. Similarly, Gaddimubarak was collected in the time of coronation ceremony of new king. Chumawan and Goddhawa were collected in the time investiture and marriage ceremonies of Royal Princes and Princesses and Gadan was levied at the time of regning King to meet funeral expenses, Darshan Bhet was collected from civil and military employees at time of their important and conformation of jobs. On the other hand, Salami was collected by local authorities in the Terai region. After the unified period, land tenure system was divided into five main forms:

Raikar, Birta, Guthi, Sera and kipat. The main sources of revenue from land were Birta and Kipat (Dahal, 2001)

The founder of modern Nepal, King Prithivi Narayan Shaha introduced pota tax in 1772, which was regarded as revolutionary measure in the fiscal system of Nepal. It was based on flat rate system rather than progressive rate principal. It was limited on small Birta owners. Though system of taxation emerged, there was no income taxation in the modern sense. (Dhakal, 2001)

2.3.3 Taxation in Rana Regime (1846-1950)

During the Rana Regime, there was no provision of effective revenue administration. The main source of revenue were land revenue, customs and export of wood, which was collected in the lamp sum, contract basis during that period and the Salami was collected from government employees as a revenue income tax. Besides these, other taxes were also collected. In those days, taxes were collected at the time of requirement because there were no formal Tax Act and finance Act. (Thapa, 1993:16)

Rana Prime ministers levied taxes for meeting specified expenditure of the royal household or extraordinary expenditures necessitated by war or other crisis rather than regular mobilization of revenue in the nation. During Nepal-Tibet war (1855/56), the first Rana Prime Minister Jung Bahadur Rana had imposed a tax on the income of selected groups. Similarly, Bir Shamsher imposed a levy of 1% on the official value of jagir assignment of government employees in 1891 to finance the transportation of water pipe supply in the capital. Another Rana Prime Minister Ranoddip Singh imposed a 50% tax on the income made by fishermen in Dhukuri from the sale of fish in 1892. (Thapa, 1993:16)

2.3.4 Income Tax in Modern Nepal

After the political Revolution in February 1951 (2007 B.S. Falgun), the role of the government had increased. The government of Nepal presented its first budget in 1952 (2008 B.S. Magh 21). The first five-year plan started in 1956 (2013-2018). Thus, the changing role of the government demanded more revenue and Nepal also felt to levy tax on income on a permanent basis. As a result, it issued first finance ordinance in 1959 (2016) to impose tax on business profit and remuneration. In 1960 (2017), the income tax act named "Business Profits and Remuneration Act, 2017 was inaugurated with the provisions of finance ordinance 1959. It was the first income tax act with 22 sections. But this act was found to be narrow and vague. So, it the Income Tax Act 1962 (2019) replaces the first one. This act continues for twelve years and also replaced later by the income tax Act, 1974 (2031) which is amended for eight times in 1977, 1979, 1980, 1984, 1985, 1986, 1989 and 1992 respectively. That tax act was replaced by new Income Tax Act 2002 (2058). This is the forth income tax act of Nepal and is in existance till date.

2.4 Gradual Development of Income Tax Law in Nepal

The F.Y. 1959/60 was the beginning of income tax act in Nepal. The Income Tax Act 1974 existed for 27 years with eight amendments. According to the section 65 of Income Tax Act, 1974, His Majesty Government had made the Income Tax Rules 1982 to implement the objectives of income tax act. Each year the finance act is passed to translate the fiscal policies and programs in the budget speech to law. It generally prescribes the tax rate and exemption limit for tax purposes and it may abolish, add or modify the provisions contained in the income tax act. The decisions of the Supreme Court also act as precedent for income tax law purpose. The notification in Nepal Gazette or circular by Inland Revenue Department clarifies and complements the legal provisions.

The Income Tax Act, therefore, has relations with the Constitution, Finance Act, Income Tax Rules and decisions of the Supreme Court. These make clear the provisions in income tax law. The development of income tax is Nepal is presented below;

2.4.1 Business Profit and Remuneration Tax Act, 1960 (2017 B. S.)

The F.Y. 1956/60 (2017 B.S.) was the beginning of the income tax act in Nepal. The First law relating to income tax was named "Business Profit and Remuneration Tax Act, 1960 and rules made there under. This act had 22 sections. With the enactment of the act, the salary tax or personal income tax was levied on those individuals whose personal income exceeded Rs. 6,000 per year. In the first three years, the exemption was Rs. 7,000. An examination of tax files in the Kathmandu district office disclosed 557 personal income tax files of individual who paid taxes in one or more years. (Cooper, 1964:4)

The following were the salient features of the Act.

1) The sources of income for tax purpose were limited to business profit and remuneration (That is the two heads of income were business profit and remuneration only)
2) The basis of calculation of the tax liability for the remuneration was the income of the current year and for business profit, it was the profit of previous year.
3) Deductions of expenses were not specified for calculating taxable income.
4) Tax on remuneration was deducted at sources. (TDS)
5) The tax officer was empowered to assess tax on best judgment estimate.
6) In case of default, fines up to Rs. 5000 were prescribed.
7) Profits from industries were granted a rebate of 25 percent and profits from small industries were granted a rebate of 50 percent.

The “Business Profit and Remuneration Tax Act” was too narrow and vague. It was limited to business profit and remuneration. High discretionary power in assessment of income tax was granted to the officers. Many loop holes for the income hiders and inadequate provisions in the act forced the act to be replaced. As a result, the income Tax Act, 1962 (2019 B.S.) was introduced.

2.4.2 Income Tax Act, 1962 (2019 B.S.)

This Act was the extension of the “Business Profit and Remuneration Tax Act” with 29 sections. It was amended in 1972. It had provision of imposition of income tax in agricultural income but this provision was abolished by the Finance Act, 1966 (2023)

The main features of the act were as follows:

1) Income was defined as all kinds of income such as profit from business, income from profession, remuneration and occupation, house and land rent, income from agriculture, insurance business, agency and any other sources.
2) The basis of tax assessment was specified on the best judgment estimate of the tax officers.
3) Provision was made for installment payment of the tax for the first time.
4) Provision was made reassessment of tax as well as rectification of arithmetical errors.
5) It had the provision regarding carry forward of losses for the period of two years.
6) Provision was made for the exemption of income tax for the new industrial for a period of not exceeding ten years.
7) The residential status of the taxpayers for the tax purpose was defined.
8) The Act granted the power to constitute the income assessment committee.

9) Deductible expenses as well as methods of calculation of taxable income were specified.

This act also has some weaknesses. The changing socio-economic environment of the nation forced to change the income tax act. As a result, the Income Tax Act, 1974 (2031 B.S.) came in to effect abolishing the existing Act 1962.

2.4.3 Income Tax Act, 1974 (2031 B.S.)

The Income Tax Act 1974 can be said to be the refined form of income tax Act, 1962. (Dhakal, 2056:11)

It contains 66 sections. It contained many provisions of the old one and added certain new provisions. This act was amended eight times for making more practical and eliminating confusing terms. Its basic framework was derived from the Income Tax Act. 1962. It retained or amended certain provisions of the old act and added certain new provisions. Some of the points of the act with amendment are as follows. (Tiwari, 1991:3)

1) This act clarified the definitions about income tax, taxpayer, year of income personal status of taxpayer, non-resident taxpayer, net income and so on.
2) Five heads of income sources were specified viz. a. Agriculture, b. Industry, Business, Profession or Vocation, c. Remuneration, d. House and Land Rent, e. Other Sources.
3) Methods of computing the taxable income from each head had been specified with deductions allowable.
4) The act made it obligatory for taxpayers to register their industries, business, profession or vocation in the tax office and any changes should be notified.

5) Carry forward of losses is allowed within subsequent three years.
6) Provision was made for self-assessment of tax for the first time in Nepal.
7) Provision was made relating to deducting for life insurance premium and contribution made for philanthropic purpose.
8) Taxpayer was required to keep accounts and records of the income and to be preserved for six years.
9) Provision was made to make agreement for a avoidance of double taxation with foreign governments.
10) Provision was made relating to reassessment or additional assessment of tax.
11) Procedures were streamlined for assessment, collection, payment and refund of tax. Powers for search and seizure also was specified.
12) Provision was made relating to departmental action in case of negligence and the penalties were increased.

2.4.4 Income Tax Act, 2002, (2058 B.S.)

The draft Income Tax Act, (2058) also proposed to bring all sources of income including capital gains into the tax net. This forth income tax act of Nepal has been made to minimize the weakness of previous act and for more collection of national receipt (revenue) for the economic development by improving collection procedure of revenue. It is also necessary to amend and integrate according to modern age with international taxation system. It is essential to make new income tax act corresponding with extended income tax scope and changing form of tax administration. Thus the new Income Tax Act 2002 (2058) was passed. It was issued and implemented from 1st April 2002 (19 Chaitra 2058) with government seal. This act made some amendments two times by the finance ordinance of 24th Ashad and 22nd Paush of 2059 B.S. (Khadka, 2001:5)

The main objectives of income Tax Act 2002 are pointed below;

1) To levy tax on all income sources and income earning transactions.
2) To impose uniform tax to all people and all sources.
3) To make income tax revenue more productive and elastic.
4) To develop the tax system by means of extended scope, clear-cut, transparent and simple procedure.
5) To make accountable improvement tax administration.
6) To reduce economic cost neutralizing income tax.
7) To emphasize statement based on accounting system.
8) To make responsible to income tax payers emphasizing procedure of self-assessment system. (Mallik, 2003:26)

This act is broad, scientific and of international standard level. The differences of this act with previous act are made clear by its salient feature, which is given below;

i) This act has included all the provisions relating to income tax. It is a law of income tax code.
ii) It has included all the financial transactions of the taxpayers considering present and future earning.
iii) Provision has made to impose tax to all income sources uniformly.
iv) Provision has been made for the deduction of all expenses relating to income earnings.
v) Provision has been made to deduct all expenses relating to each income in accumulation from taxpayer's income.
vi) Carry forward of losses is allowed for the period of four subsequent years. This limit is extended up to five years for banking and insurance business.

vii) Provision of tax incentives has continued for infrastructure instructions, electricity projects and special industries.

viii) It has accepted self-assessment system absolutely. Provision has also made to accept the statement submitted by taxpayer as tax assessment and in case of non submission of the statement, the advance tax payment made by taxpayer is taken as assessed tax amount.

ix) It has clearly included the right and duties of taxpayers.

x) It includes general anti-avoidance rule, control of transfer pricing, control of thin capitalization and control of dividing stripping to control tax evasion measure.

xi) Provisions have made to claim for deduction of pollution control device and research and development expenses.

xii) It has classified the taxpayers in to the natural person and entity; Entity includes company, partnership, and trust and so on.

Special Provision for Banking and Business

Income Tax Act, 2002 has made special provision for banking business (section 59). According to this section, provision given to that sector is as follows.

1) Prime Introduction: Banking business refers to the banking transaction of affiliated bank and financial institution in accordance with prevailing law according to Income Tax Act, 2002.

2) Banking transaction refers accepting deposits for making loan and investment paying back it at the time of demand by saver according to Commercial Bank Act, 1974 (2031) and finance Company Act, 1983.

3) Provision for Risk Bearing Fund: Any provision debited in the profit and loss account is not deductible according to the Income Tax Act, 2002. However, the financial ordinance 2059 has emended it and provision has

been made to claim for deduction of risk bearing fund up to 5% of outstanding loans that was only 3% according to Income Tax Act, 1974.

4) Written off Loss: Loan loss of banks can be written off in compliance with NRB guidelines and it can be treated in the debit side of profit and loss account as expenditure for carry back of losses but it is not allowed if this amount has already deducted from income as risk bearing fund.

5) Carry Forward of Loss: Loss of any year from banking business can be carried forward to the past five year for deduction of it from incomes of those years.

6) Interest Suspense: As per direction by NRB to the banking, no interest can be treated as income on the accrual basis. Interest suspense account should be opened if the interest earned but not received in each within one month. This type of income is given tax exemption by the Income Tax Act, 1974 and it is continued by this act issuing the finance ordinance 2059.

2.5 Concept of Corporate Tax

A company or a corporate body is a voluntary association of persons formed to run business activities for fulfilling the objectives of earning profit by collecting capital and selling shares. A person or some persons interested to carry on any business or mercantile activity or other lawful trade with the motivation of earning profit by contributing money or money's worth incorporate corporate structure.

Corporate bodies conduct business and generate profit. Corporate tax is a tax levied on corporate bodies contrast to unincorporated enterprises. So corporate tax is charged to the profit earned by corporate bodies in a particular time period. The history of corporate tax is not long so far. It was started from 1909 in USA when 1% excise was levied on corporation i.e. companies on the ground of the privilege enjoy. After this all the developing countries followed the corporate tax. Now it is contributing a substantial amount of revenue to the state of treasury of the countries. Corporate tax rate is being ups and down from its very beginning. Corporate tax was very low in its initial period. It increases vehemently later on after First World War and started to be down turned since 1980s.

American Chief Justice Marshal defines company or a corporate body as a person, artificial, invisible, intangible and existing only in the eyes of law. Being mere creation of law, it possess only those properties which the charter of its creator confers upon it, either expressly or identical to its very existence. The above definition clears that a company or a corporate body can be defined as a voluntary incorporated organization for profit. It is an artificial legal person with a perpetual, succession, capital, have been divided into transferable shares with limited liability. It has own property. It can execute contract, raise debts and generate profit.

2.5.1 Development of Corporate tax in Nepal

Nepal has started informal taxation already from the beginning of Lichhavi Kal. Although Nepal has a long history of taxation the history of corporate tax is not so far long. Corporate tax was introduced only in 1060 after enacting the "Business Profit and Remuneration tax Act 1960. At the beginning of corporate tax it was not differentiated from personal income tax. The same personal income tax rate was imposed to the entire taxpayer with progressive and exemption limit prescribed by the finance act 1960. In F.Y. 1965/ 66 the tax exemption given to companies was withdrawn.

Nepal originally combined corporate income tax with individual income tax. The same rate structure was designed for corporate income and other incomes for many years. In 1986/87, a flat rate corporate tax was introduced for government corporation and public limited corporation listed with the security exchange centre. Corporate tax was extended to private limited companies in 1993/94 and partnership firms in 1995/96. (Khadka, 200:5)

Income Tax Act, 1974 came into effect with some changes and new provision in place of old one. This act introduced a separate provision to companies. Similarly, the finance Act 1985 made a provision of giving 5% tax rebate from higher marginal rate of 55% to listed public companies and government enterprises. The F.Y. 1986/87 changes the nature of tax rate to the corporate bodies (companies) from progressive tax rate to flat tax rate. In this time the tax rate was 40% flat rate to all listed companies. The same finance act imposed tax on dividend also to be deducted at source at rate of 20%. But the dividend tax system was changed exempting dividend to a level of 85% in 1987/88 and cent percent in 1990/91. Compulsory self-tax assessment system for public and private limited companies was introduced in the Finance Act 1992. The additional change of taxing corporate income at flat rate to the private limited company was enacted from the financial year 1994/95. This change abolished the discrimination between private company and public company. Another major change carried out in the F.Y. 1998/99 was the inclusion of dividend of non-industrial companies within the tax net. The initial corporate income tax rate in 1960/61 was 25%. It was increased to 60% in the F.Y. 1975/76. It was dropped to 50% in 1979/80 and continued to 1981/82. Once again, the rate increased up to 55% in 1982/83 and was stable for 3 years i.e. up to 1986. And declined then after, to 40% and 30% for up to 1991/92 and now this rate is 20% for special industry and 25% for general industry and 30% for bank and finance companies.

2.5.2 Corporate Tax Rate Structure in Nepal

Developing countries like Nepal needs to boost up their economic conditions by developing industries and trade within the country. Tax rate is the base of measurement of tax liability. It should not be high only for maximum revenue realization but should be activator for the private investment. Imposition of tax on corporate profit was started with the enactment of the Business Profit and Remuneration Tax act, 1960. The starting corporate tax rate was 25% and it was levied on progressive way. The tax amount was calculated on different slabs before fiscal year 1985/86. The corporate tax rate structure was combined with individual tax rate structure. The reason was the number of companies was limited and family generally managed private companies. In the year 1985/86 the progressive tax rate structure was abolished in case of government enterprises and public limited companies listed in Nepal Stock Exchange because enterprises used to split in to different units to the private companies also was abolished in the fiscal year 1995/96. Thus, flat rate system has been continued for all corporate bodies since the fiscal year 1995/96.

In the fiscal year 1975/76 the corporate tax rate was increased up to 60% the maximum rate from the 25%. During 1960/61 to 1975/76, increment of rates ware made three times. After fiscal year 1975/76, the tax rate again decreased up to 51% and 50%. This rate was again increased to 55% and remains continued from fiscal year 1982/83 to till 1987/88. In the year 1987/88, the listed public companies were levied 10% less than others. This concession was given to such companies by only 5% in the year 1985/86. After the fiscal year 1987/88, the tax rate was continuously decreasing. Now it is 20% to industry (except cigarette and alcohol), 25% to general companies and 30% to bank and finance companies. Special fee 3% of taxable income was levied to all corporate bodies. Now it is decreased to 1.5% as surcharge (additional income tax since F/Y2062/63)

Table No. 2 Corporate Tax Structure of Nepal

Year	Marginal tax rate		Nature of Tax rate
	Pvt. Company	Public company	
1960/61-1962/63	25	25	Progressive
1963/64-1964/65	30	30	"
1965/66-1966/67	40	40	"
1967/68	55	55	"
1968/69-1974/75	55	55	"
1975/76	60	60	"
1976/77-1978/79	51	51	"
1979/80	50	50	"
1980/81-1981/82	50	50	"
1982/1983	55	55	"
1983/84-1984/85	55	55	"
1985/86	55p	55f	Progressive & flat
1986/87-1987/88	55p	50f	"
1988/89-1989/90	50p	50f	"
1990/91-1991/92	40p	40f	"
1992/93-1994/95	35p	35f	"
1995/1996	33	33	Flat
1996/1997	30	33	'
1998/99-2002/03	20-25&30	20-25&30	Flat rate

Sources: 1. Kandel, P.R. (2000) corporate tax system and Investment Behavior in Nepal.

1. Budget speeches, 2002/03

Note: 20% tax rate for special industries.

25% tax rate for general industries producing Liquors and tobacco.

30% tax rate for non-industries for banking, finance and insurance business.

2.5.3 Tax incentive

Tax incentives are such facilities or concessions given to the corporate bodies. Tax incentive is a phenomenon developed specially to accelerate the slow rate of investment. The main objective of tax incentive is to increase saving and encourage to investment in desired sector. It encourages investing in selected manufacturing activities and helps for utilization of domestic resources.

The tax incentives are becoming an important and getting wide support in short period. Especially developing country like Nepal, the increase in corporate, investment is the sign of socio-economic development of the nation. Development of the industry is necessary to utilize the natural resources. It can be successful after encouraging investor to invest in this area. Investors desired can be fulfilled by giving tax intensives because investors are interested to invest only such that cases when the after tax profitability becomes high.

A variety of incentives laws prevail in different countries influenced by their economic and political nature. Among different varieties of incentives the more popular incentives in different countries of the world are;

- Tax holiday (investment incentives)
- Set off and carry forward of losses
- Depreciation allowances
- Tax rate deductions

Incentive tax holiday is the holiday from tax a certain period of time. It is one is one of the most popular of all the tax incentives. This incentive is mainly concerned with new companies and short-lived project in the industry sector. "Such a relief on tax is applicable on profit earned from new investment and it will automatically terminate after holiday period." The aims of this incentive are job creation, technology transfer, industrialization, promoting industry, regional development, research and development etc. After the expiry of tax holiday period these corporate bodies will be subjected to the rate of taxation according to the tax act (rule).

Set off and carry forward of and carry forward of losses in another technique of tax incentive. If there is losses under the one sources and profit under another sources of it head is set off against the later. The net loss of this year can be carried forward in further years for set off against the income of subsequent year. Different countries are giving such incentives in terms of scope, condition and time. Most of the countries allow to deduct losses or carry forward of losses for subsequent 5 years. In Nepal as per Income Tax Act, 1974, losses were allowed to carried forward and set off in the following three years, which was only two years allowed by income tax act 1962. Now new Income Tax Act, 2002 has increased this period up to 4 years for general business and 5 years for bank and insurance.

The next incentive system depreciation allowances mean higher depreciation in initial year and gradual decrease in latter year. It is also included allowing the cost of fixed assets to be depreciated with in a shorter period than its service life. Written down value method and double decaling methods of depreciation do this work in better way.

The last but not least method of providing incentive is reduction of tax rate. This method mainly focuses on reduction of statutory rate of tax. It is very simple and economic method. However reducing tax rate reduces the government revenue, it treats all the firms equally whether large or small, new or old, and short levied or long levied capital intensive or labor intensive and located in urban or rural areas. This incentive system is a phenomenon. Almost all the countries of the world are following this system during these days and cutting their corporate tax rate vehemently.

Among these type of investment incentives, investment allowance is mostly used by British commonwealth nation like Coast and Central Africa, Sri Lanka, Canada, Australia etc. besides these Belgium, Germany, Japan, United Kingdom, Brazil, Malaysia, China, Singapore, Taiwan, South Korea and Egypt are also using this method to argument their investment (Kandel 2001:61)

In some developing countries like, Philippines, Mexico etc. the incentive is mainly in the form of tax holiday. A combination of tax holiday with investment allowances and other rebate is also common in many countries. Aforesaid tax incentives have always been the important parts of corporate tax system because they are important instruments in accelerating the pace of economic growth through mobilizing saving and investment. The type, size and magnitude vary according to the needs and aspiration of the people of different countries. (Poudyal 1993:40)

2.5.4 Tax Incentive in Nepal

The corporate sector is in the initial stage of development in Nepal. The performance of corporate sector especially the industry is very poor. To develop the corporate sector in Nepal, many incentive provisions are providing by different government laws. They are Industrial Enterprise Act, 1992; Nepal Petroleum Act, 1993; Electricity Act, 1992 and Foreign Investment and Technology Transfer Act, 1992. Nepal Petroleum Act, 1993 has provided certain relief on tax rate to petroleum industries. Similarly, Electricity Act, 1992 has given certain facility to the hydro electronic power in Nepal and Foreign Investment and Technology Transfer Act, 1992 has made the provisions regarding tax relief to foreign investors.

Most important law regarding to the corporate bodies in Nepal is Industrial Enterprises Act. The main agenda of this act is to provide fiscal incentives in to the industries. Up to this date, Nepal has experienced 4 Industrial Enterprises Acts. They are Industrial Enterprises Act, 1962; Industrial Enterprises Act, 1974; Industrial Enterprises Act, 1981; and Industrial Enterprises Act, 1982. In relation to tax incentives provided by them, first Industrial Enterprises Act 1962 made the provision of 10 years tax holiday for new industries; tax rebate up to 25% of the tax liability on the discretion of HMG/Nepal to existing industries; full or partial rebate of the tariff for exporting goods and importing machinery, parts and raw materials. The main type of incentives provided by Industrial Enterprises Act, 1974 were up to 18 years tax holiday to different industries established in different part of the countries; investment allowances and depreciation facility to extension and modernization; relief of excise duty, import duty etc. Accordingly, the main types of tax relief provisions appended in Industrial Enterprises Act, 1981 also were not so much different from that of its predecessors. It also included up to 12 years tax holiday to industries. Income tax rebate of up to 50% for export, 15% investment allowances to additional investments, only 1% levy for import of machinery spare parts and raw materials; excise exemption to different types of industries; exemption of sales tax to cottage industries on import of machinery, spare parts etc. and domestically produced goods. Apart from these, there was also the provision of charging depreciation on assets on depreciating balance method as 5% on building, 25% on Computer & accessories, & furniture & fixtures, 20% on Machinery, 15% on other assets apart from the one mentioned earlier and life of 5 years is assumed for intangible assets.

Industrial Enterprises Act, 1992 avengement 1997 has given various tax related facilities to the industrial communities. They are as follows:

- Complete exemption of any type of income tax, sales tax, excise etc. for cottage industries.
- Specifying as maximum rate of tax to industries except those related to tobacco and alcohol.
- Ten years 50% tax holiday to the national priority industries related to the construction of roads, bridges, tunnels, ropeways, flying bridges, trolley buses and trams.
- Income tax rebate of 60%, 50%, 25% and 10% and excise rebate of 35%, 25%, 15% and 10% to the industries established in remote, underdeveloped, partially developed and developed area respectively except the industries based on tobacco and alcohol.
- 25% tax exemption for ten years to those industries, which are not related to tobacco and alcohol and are established in underdeveloped area stated in Appendix-III of the act.
- Five plus three years sales and excise rebate to the fruit processing and fruit based wine producing industries located in remote areas.
- Investment allowance of 40% extended fixed assets investment if the firms increased its capacity of line production by more than 25% of original level.
- Deduction of 50% pf expenditure made for pollution control from taxable income. ‘
- Deduction facility of 5% and 10% of gross income for promotion and development of technology respectively from net income.
- 30% tax exemption for industries, which are not related to tobacco and alcohol and are established in most underdeveloped district stated in Appendix-III of the act.
- 20% tax holidays for those industries, which are not relates to tobacco and alcohol and are established in under undeveloped district stated in Appendix-III of the act.

2.6 Tax Evasion and Avoidance

Tax evasion and avoidance both are major causes to make low income tax collection. Income tax checks the inequality between high and low income people or firms. It helps government in the movement of resources from the private to public sector. Income tax can only achieve its goal if its evasion and avoidance is controlled.

2.6.1 Tax Evasion

Tax evasion is eliminating the tax burden and liability by dishonest manner. It means fraudulent, illegal useful and elaborate acts of taxpayers culminating in the volition of the civil or criminal provisions of the tax laws. It implies maneuvers involving an element of concealment, deceit, misrepresentation of facts, falsification of accounts and downright fraud resulting from conscious effects of the taxpayers to evade payment of tax legally due. Tax evasion may arise from weak enforcement, inadequate tools or resources of administration and low taxpayer's integrity or moral. Tax evasion may involve;

- Omission of taxable income.
- Less receipt.
- Artificial expenses.
- Concealment of a source of income.
- Incorrect claim for allowances and deduction.
- Fictitious transactions.
- Over and under invoicing.
- Maintenance of multiple sets of accounts.
- Artificial contracts.
- Misrepresentation of facts and in formations.

Tax evasion can be several types;

i. Unilateral: It is evasion of tax by taxpayer himself.

ii. Bilateral: It is evasion of tax with the assistance of tax officials.

iii. Trilateral: It is evasion of tax from the collusion of tax auditors and taxpayers.

iv. Multilateral: It is evasion of tax from all parties involved from government to taxpayers.

Tax evasion is an illegal work so it has to be penalized by court. Failure to submit income statement tot ax office and failure to make payment of taxes because of negligence are also regarded as tax evasion.

2.6.2 Tax avoidance

Tax avoidance refers to reduction of tax liability through legal means. It means making good use of legal loopholes shortcutting and weakness of tax law. It is not illegal but unethical. It has become a science and arts with its own investors and practitioners. “A taxpayer is entitled to so arrange his financial affairs so as to take the maximum advantage of the law and its weakness to reduce or prevent its liability.

Some methods of tax avoidance mentioned by Dr. G.R. Agrawal in his book “Resource Mobilization for Development” are as follows;

- Registering firms, which are not genuine, composed mainly of family members, to reduce incidence of tax.
- Diversion of income or assets to different taxable entities so that lower tax rate may apply.
- Transfer of income to wife or minor child with out adequate consideration.

- Transfer of assets and/or income to non-residents.
- Investment in capital assets. In Nepal capital gain are not taxed.
- Transferring business to tax havens.
- Payment of salaries, interests and other benefits to family members.
- Expenses camouflage.
- Purchase of such firms, which have huge amount to be carried forward as losses.
- Formation of rules and other philanthropic type institutions, which are exempt from, tax but whose benefits do the family members derive.
- Use of nominees in Nepal or in other countries by non-residence through collective agreements when undertaking business transactions.
- Factitious contracts in the name of international enterprises, such contracts stipulate that delivery will be made at Indian railhead points. This income there by is not received in Nepal.
- Representing international forms in Nepal for supply and other purpose and getting commission for such representation.
- Sales cum dividend deals.
- Transitions in fictitious names etc.

Tax avoidance can thus be defined as any planning of tax which through done strictly according to the legal requirement but defeats the basic intension of the legislature behind the tax law. It is legally permissible but unethical.

2.7 Tax Administration

Tax administration implies the management of affairs related to tax. A sound system of tax administration is pre-requisite to assess the taxation policies of the government. For the success of tax administration of any government different constituents are established and these plays significant role such as executive, legislative, reporting, auditing etc.

2.7.1 Income Tax Authorities

Income tax is administered directly by the Inland Revenue Department. It is responsible for the implementation and administration of the Act. His majesty's Government is the highest authority of the tax offices of the Department and prescribed their jurisdiction by notification in the Nepal Gazette to facilitate the Department in fulfilling its responsibilities. The following officers and other staff may be deputed in the Department:

- A Director General
- Deputy Director General in the numbers as may be required
- Chief Tax Administrators
- Directors
- Chief Tax Officers
- Tax officers
- Other Officers and
- Other Staff

The Ministry of Finance is at the apex administration. The Ministry carries out the functions related to taxation on behalf of HMG. The Revenue Department of the Ministry is responsible for formulating tax related policies and coordinating the activities of all Revenue Departments. Similarly Custom Department, Revenue Investigation Department and Revenue Administration Training Centre are also involved in the administration of income tax.

2.7.2 Rights of HMG/ Nepal

Income Tax Act, 2058 has empowered HMG/ Nepal as regards to the implementation of the tax law, the rights of HMG/ Nepal with respect to ITA, 2058 are;

1) Right to make double tax avoidance treaty with other countries to avoided the situation of double taxation.
2) Right to establish or remove tax office for the purpose of collecting tax, It has also the fight to appoint tax officers and delegate powers.
3) Right to establish or remove of donation given to tax exempt organization by publishing a notice in Nepal Gazette.
4) Right to make rules regarding tax for fulfilling the objectives of the Act.
5) Right to make changes as required in schedules other than schedule 1.
6) Right to remit in whole or in part any tax payable by a person if the Tax cannot be collected.
7) Right an order or direction to Inland Revenue Department for the purpose of making tax administration effective.

2.7.3 Power of Department

Inland Revenue Department (IRD) can exercise the following power given in ITA, 2958 and Income Tax Rule, 2059:

i. To take an official against its employees.
ii. To exercise power of the court for the purpose of this Ac.
iii. To develop and issue directives as required.
iv. To order for payment of penalty amount.
v. To decide an exempt amount.
vi. To specify accounting methods.
vii. To specify about the long term contract.

viii. To characterize the amount in advance on the basis of arm's length principle.
ix. To approve retirement fund
x. To give permanent Account Number (PAN) and amend it as per request.
xi. To provide tax clearance and tax exemption certificate.
xii. To specify taxpayers who are not required to submit returns.
xiii. To specify the place of auction.

2.7.4 Right of Direct General (DG)

Director General subject to direction by HMG can:

i. Exercise any power granted to the Department under the Act.
ii. Delegate the exercise of any of the power to another officer.
iii. Where there is no tax officers, assign any of the officers in the civil service to exercise all or any of the powers other than the power:
    - To issue public circular.
    - To prescribe documents.
    - To stay or otherwise affect a review able decision.
    - To allow or disallow the objection by any person in whole or part.
    - To compound an offence and
    - To authorize any officer.

2.7.5 Right of Deputy Director General (DDG), Chief Tax Administrator, Director, Chief Tax Officer or Officer or Officer appointed as the Chief of a tax office may:

1. Exercise any power granted to the Department under this Act other than the power:
   - To issue public circular under section 75.
   - To prescribe documents under section 77.
   - To stay or otherwise affects a revisable decision under section 115.(5)
   - To allow or disallow or disallow the objection by any person in whole or part under section 115(7).
   - To compound an offence under section 129
2. Delegate the exercise of any such power to another tax officer.

2.7.6 Rights of Other Officers

An officer of the Department other than the Director General, a Deputy Director General, Chief Tax Administrator Director, Chief Tax Officer appointed as the Chief of a tax officer may:

1. Exercise any power granted to the Department than has been delegated to the officer other than.
   - To issue public circulars under section 75.
   - To prescribed documents under section 77.
   - To say or otherwise affect a review able decision under section 115 (5)
   - To allow or disallow the objection by person in whole or part under section 115(7)
   - To compound an officer under section 129 and
   - To authorize an officer under section 82 or issue a notice under section 109.

2.7.7 Right of Taxpayer (Assesees)

A taxpayer means a person (an individual or entity) whom the tax imposed on and realized from as per Income Tax, 2058. As per section 74 of the Act, the taxpayer with respect of paying tax is entitled to enjoy the following rights:

1) Right to get respectful behavior.
2) Right to receive tax related information as per prevailing laws.
3) Right to get opportunity of submitting proof in own favor in respect of tax matter.
4) Right to appoint lawyers or auditors for defense and
5) Right to secrecy in respect of tax matters and keeps it inviolable.

   Besides these, the taxpayer can enjoy the following rights:

6) Right to obtain clarification on personal (advance) rulings.
7) Right to get refund of excess tax paid
8) Right to appeal to review the decision.
9) Right to receive public circulars.
10) Right to extend time to file return.

2.8 Problem Associated with Tax Administration in Nepal

The Government needs huge amounts for the expenses to be made in developing and operation. Each year the estimated expenditure exceeds over expected revenue, that arises revenue gap and it needs to borrow foreign loans. The income tax is only justifiable to increase the resource mobilization in the nation internally. However, due to poor earning capacity of people it is difficult to raise the contribution ratio of income tax in the total revenue. On the other hand, most of people who are earning significant amount are beyond the income tax net. The income tax system in Nepal has been facing many problems. Inefficiency of income tax administration is one of the reasons. Tax administration is a complex and difficult technical matter. There are explained some problems including passed period.

2.8.1 Failure to Locate New Taxpayers

Govind Ram Agrawal has pointed out the relation to the location of new taxpayers in his book "Resource Mobilization in Nepal" as "Tax Administration in Nepal lacks and up to date roll of existing as well as potential tax payers." (Agrawal, 1980:109) Tax administration set target to collect income tax in certain percentage of GDP each year, and makes policy to extend the scope of taxation. But the target has not been fulfilled. The major problem is the location of new taxpayers in the case of non-resident and non-citizen persons who are really outside the income tax net. This is due to open border with India. Similarly, self-employed persons as professionals and skilled persons have also remained outside the effective react of income tax net. Brokers, speculators, foreign goods dealers, suppliers in big hotels, tourist guides, insurance agents and persons remaining outside the net income tax. Administration deficiency, poor taxpayers' morality and compliance about the income tax payment are the major responsible factors for problem of failure to locate the new taxpayers.

2.8.2 Failure to Maintain Proper Account and Records

Most of taxpayers in Nepal do not maintain account in proper way for the income tax purpose. They show hesitation in submission of accounts and tax returns in the Inland Revenue offices. On the other hand, large numbers of private business entities submit false income statements for tax purpose even through they maintain accounts of their business transactions, they make two sets of accounts and hide the real statement. That is a reason why the income tax officers fail to find out the true and fair view of the financial state of affaires of taxpayers. There are many reasons, which encourage making false accounts for tax purpose. Some reasons are stated below.

a. Attitude of the Tax Officers: The attitude of the tax officers is responsible for failure to maintain proper accounts and records. Generally, tax officers reject the accounts submitted by taxpayers on the plea that they are not acceptable. They are reluctant to verify the accounts in depth investigation. The reasons are: some tax officers are lazy and most of tax officers have no competency of inspecting accounts for the collusion with taxpayers to mutual benefit. Anyway, this type of negative attitude of tax officers is not mutual benefit. Anyway, this type of negative attitude of tax officers is not conductive to the development of the habit of maintaining account by the taxpayers.

b. Ineffective Use of Sanction: The ineffective use of sanctions provided in the law against those taxpayers who fail to comply with the accounting and reporting requirement of law has encouraged non-maintenance of a accounts.

c. Lack of Intermediaries: Professional accounts, tax lawyers and tax consultants are the intermediaries and they make valuable assistance in the maintenance of accounts. They provide professional services to the taxpayers for the consultation of tax provision and maintenance of accounts and proper records in proper way, however, such intermediaries have not received adequate encouragement and support from the tax administration.

d. Assessment by Committee and Best Judgment: Income tax is assessed under different methods in Nepal viz. committee assessment, best judgment assessment, accounts assessment and self-assessment system. Self-assessment system was started from F.Y. 1992/93 in practice. Mostly the committee assessment and best judgment assessment have been applied commonly. More than 60% of assessments of tax liabilities are made by committee method in Nepal. However, more than 12% of tax assessment is made by the best judgment system. The account method of assessment is applied in low percentage say below 8%. Thus mostly committee and best judgment methods are in use. Indeed, most of taxpayers seem to prefer these methods because there is no limit as to the amount of income, which can be assessed under these methods. The tax officers also enjoy discretionary powers while making assessment under the best judgment methods. This method encourages both taxpayers as well as tax officers to make collusion between them for financial benefit and it increases dishonest taxpayers as well as corrupts tax officers. Thus. Tax assessment by committee or best judgment method has been discouraging maintains of proper accounts by taxpayers. This is harmful to the tax administration.

2.8.3 Assessment Delays

Tax assessment is the computation of taxable income and tax liability of a taxpayer for certain period by application of government rates. Assessment procedure starts with the submission of tax return. It is scrutinized, verified and audited for checking accuracy and reliability of contained information about income and expenditure. Assessment of tax liability is very time consuming in Nepal. This is a serious problem in the tax administration of Nepal. The major reasons for assessment delays are listed below.

a. Defective assessment procedure.
b. Delays in filing of income tax returns.
c. Non-Maintenance of accounts by taxpayers.
d. Poor recording and filing system in Inland Revenue department.
e. Unclear tax provision.
f. Irregularities and negligence of tax personal.

All these reasons are equally responsible for assessment delays in tax administration.

2.8.4 Collection problem

The main measurable factor performance of tax administration is collection of tax revenue. From the point of view, it is seen that the performance of tax administration is not satisfactory because of low collection of income tax. Notwithstanding, the income tax act has prescribed stiff fines and penalties for non-payment of tax; the collection situation has been worsening. The collection problem has been continued from the beginnings of income tax administration due to various reasons which are given below.

I. Undue delays in assessment: The traditional habit of undue delay in assessment has been serious obstacle in the collection of revenue in Nepal.

II. Non-compliance by tax officers: Many taxpayers do not submit or pay income tax in due date. Reluctance to use fines and penalties encourages them keeping a defaulting in payment of tax.

III. Change taxpayer's identity: The identities of firms and their proprietor have changed frequently in Nepal. This has been constrained in collection of taxes. Some dishonest firms. This is also reason for collection delinquency.

IV. Weakness in marketing fines and penalties: Although the income tax act has made provision of stiff fine and penalties for non payment of tax. Inland Revenue offices have been reluctant in making fines and penalties to them who do not submit or pay income tax in due data.

V. Lengthy procedure in payments: There are lengthy procedures of completing work in all the government offices. Same reason exists in the payment of income tax. Taxpayers should deposit tax amount in NRB by filing five vouchers. This is rigorous to the taxpayers and it has adversely, affected in revenue collection.

VI. Undue delay in settlement of appeals: Appeals filled by taxpayers are not settled in time in Nepal. This freezes the tax amount in a deposit account.

Besides aforesaid reasons of collection problem, some other are listed below;

i. Lack of collection responsibility.
ii. Untimely deposit of tax collection at source.
iii. Defective accounting system in Inland Revenue offices.
iv. Failure of public sector enterprises to pay the taxes.
v. Tax holiday granted to new industries.

2.8.5 Poor Taxpaying Habit of People

Traditionally, Nepalese people have no consciousness of income tax. They have been paying indirect tax and land tax without hesitation because of unfeeling of payment. Many people still perceive that income tax is a burden and an unnecessary payment. Voluntary compliance, the corner stone of effective tax administration is poor in Nepal. Most of people who earn considerable amounts hide the income and do not pay the tax.

In the developed countries, people involve in voluntary compliance for tax payment. They feel that not to pay income tax is a social crime. But in developing countries like Nepal, tax liability is hidden and this type of practice is taken as a brilliant work. On the other hand, the government is trying to extract compulsory payment out of income of taxpayers through income tax law. The contribution of income tax to the national receipt is reactively low in the developing countries in comparison with developed countries. To increase the contribution on income tax to national revenue for the economic and socio development taxpayers need to be persuaded and influenced to meet their tax obligation in a co-operative sprit. This requires integrated programs and taxpayer education. However, lack of education of taxation to the taxpayers has been increasing non-voluntary compliance in tax. On the other hand, tax administration experts think that any taxpayer is compelled to pay income tax by the law. This is not correct through because habits of people need to be improved through good education system rather than by making force.

The major responsible factors that make poor tax paying habits of people in Nepal can be listed as follows;

1. Negative attitudes of tax personnel.
2. Vague and complicated laws of taxation.
3. Lengthy assessment procedure.
4. Lack of taxpayer's education.
5. Weakness in enforcement of fines and penalties.
6. Lack of research in tax matters.

2.9 Review of Related Studies

Since the period of introduction of income tax system in Nepal, many individuals as well as some institutions have made efforts on study of taxation the ways for the improvement of income tax system in Nepal in every aspect of income taxation. Many books, research reports and article have been written and published in this respect. The researcher had consulted books, theses and some articles concerning with income taxation during the theses writing. Some of them are presented in brief below;

Govinda Ram Agrawal presented the research report entitled "Resource Mobilization for Development: The reform of income tax in Nepal" which was published by the CEDA kathmandu in July 1978. This research work was the first comprehensive study on the income tax in Nepal. In the research work, he analyzed various aspects of income tax system of Nepal such as role of income tax, legal aspect of income tax and administrative aspect of taxation in Nepal. In this report, he showed the cause of problems facing by tax authorities in the tax administration. As per his study, the main causes of administrative problems were undue delay in tax assessment, failure to maintain proper account by taxpayers, failure to maintain proper records by tax offices, failure to locate new taxpayers, unfriendly behavior of tax officials to the taxpayers, assessment under the best judgment etc. he also showed the main reasons of assessment delays in Nepal. As mentioned by him delays in filling of returns of income, delay in settlement of appeals defective assessment procedure, lack of proper taxpayer information and failure to maintain the proper accounts and records by taxpayer/tax offices. He also found the buoyancy of income tax with respect to GDP for the period 1967/68 to 1975/76 and elasticity of income tax. He also showed about 2.18 buoyancy and 2.01 elasticity of income tax.

The other book named “Income Tax System in Nepal” written by Narayan Raj Tiwari published in 1978 described the income tax in general. This book is consisted the historical background of income tax in Nepal. This book therefore was useful to understand the theoretical aspect of income tax law only because it failed to give the fact about the role and numerical information of income tax in Nepal.

Surendra Keshar Amatya, Dr.Bihari Binod Pokheral and Rewanta Kumar Dahal (2004) wrote a book entitled “Taxation in Nepal” Mr. Amatya, Pokheral and Dahal, described the provisions made under income tax laws. In their books, Mr. Amatya, Pokheral and Dahal, has described about income tax and its development in Nepal, tax accounting, quantification, allocation and characterization of amounts, exemptions, concession, facilities and tax rates, expenditure expressly disallowed for deduction capital or revenue incomes and expenditures taxpayer, special provision for natural person and entity, income heads and sources, income from employment, income from business, set-off long back and carry forward of losses, income from investment, net gain from disposal of assets and liabilities and capital gain taxation, total assessable income, taxable income and tax liability, international taxation, form of documentation, PAN and maintenance of documents, income return and tax assessment payment, collection and refund of tax, tax administration, rights and duties of taxpayers etc. This book has been written to fulfill the course requirement of Trivhuvan University. It is based on the syllables of Bachelor level of management, law and CA and it is also for master level of management and law. This book is informative rather than analytical. They have also included numerical problems in regard to income tax assessment. The student of Bachelor and master can get assessment system. But this book has not analyzed the importance of income tax, problem and defects in Nepalese income tax system.

Puspa Raj Kandel also presented the Ph.D. thesis entitled “Corporate Tax System and investment Behavior in Nepal” in 2000. He undertook the research work to find out the problems relating to corporate tax, which blocks the development of private investments. The main objectives of this study were to evaluate the corporate tax system in general, to examine the sensitivity of certain policy like inflation, capital gain tax, dividend tax and interest tax etc. based on their impact on tax burden. He showed the relationship of private investments with average effective tax rate (AETR), marginal effective tax rate (METR) and tax incentive in Nepal. He found that the METR for debt-financed project are almost negative (i.e.-1.7%) and positive for equity financed project and debt-equity ration project by 27% and 19% respectively. He had also found the impact of inflation to the METR. According to him, the statutory tax rate deduction had impact private investments by 60% to 20 %. In this regard, he had showed the adjusted R^2 value 0.87 at 5% level of significance. He had concluded that the statutory tax rate was in moderate level under all financial options: debt, mix and equity i.e. it was not much distort. The relationship between inflation rate effective tax burdens in Nepal

Above studies shows that Income Tax is main source of government revenue. It is useful to balance economic development. Nobody can doubt that, the equal distribution of income is also possible through progressive income tax. Nepal has adopted the income tax system for last four half decades. But Nepal's past experience shows that the government is unable to maximize the share of income tax to the public fund as per expectation. Merchant Banker plays a vital role in economic and financial development of the country. Because they are profit oriented entities so they must pay income tax out of their net profits. Here is necessary to review of Merchant Bankers.

"The term 'Merchant Banking was originate in the 18th and early 19th centuries in the United Kingdom when trade between countries was financed by bills of exchange drawn on the principal merchant houses with the increase in international trade, the established merchants started the practice in lending their names to the new comers and accepting the bills of exchange on their behalf. They would change a commission for the purpose and thus acceptance business became the hallmark of Merchant bankers. Once these banks had gained the confidence of the government, they also entrusted with the job of issuing bonds in the London market"

Merchant Banking service was introduced in the different period in different countries. It was emerged in the early 19th century in the USA with the introduction of Blue Sky Laws to protect investors from the promoters and security salesman. In India merchant-banking activities was originated only after restoration of independence. After the Banking Commission in 1972, Indian banks started merchant banking service as part of their multiple services. State Bank of India in 1972 with its Merchant Banking Division was the first bank to offer the merchant banking services. (B.C. Lakshmanna & C.N. Krishna Naik, "Merchant Banking in India", Deep & Deep Publication Ltd 2002 p.88

About Nepalese concept, it hasn't so long background about financial system. Before the establishments of "Tejarath Adda" during the period of Rana regime pass the unauthorized sectors like moneylenders, goldsmiths, landlords have their universal domination on the financial matter. They used to charge very high interest rate. “Tejarath Adda” may be regarded as the father of the modern banking institutions in Nepal.In the context of Nepal, Merchant banking exists from the establishment of Nepal Bank Ltd. in 1994 B.S. existence was in a crude form. After the restoration of democracy in 2046 B.S. and an announcement of government’s economic liberalization policy, private sector investors are attracted to invest in different organized commercial ventures. As a result, lots of public and private limited companies were established in a very short span of time to reap benefit of economic liberalization policy of the nation.

According to Mr. Ramesh Kumar Pokheral in his article “Merchant Banking Service in Nepal” in Banking Prabadhan, 2057 vol.11 has mentioned on Regulatory Aspect of Merchat Banking in Nepal. Merchant Banking is a new concept for Nepal. Its role as an important financial intermediary cannot be challenged from anywhere in the growing financial system of Nepal. Although a few financial institutions (basically finance companies) are involved in different merchant banking activities, there is no clear definition of merchant banking in finance company Act, 1986 and no specific legal provision to be complied by merchant banker. However Bank & Financial Institutions Act, 2063

permits bank & financial institutions to sell, purchase the bonds issued by his Majesty’s Government also of other companies or institution, to underwrite them.

Since there is no separate entity to carry out the merchant banking activities in Nepal, these activities are associated with other transaction of finance companies.

CHAPTER – III

RESEARCH METHODOLOGY

Methodology is the research method used to complete the study systematically and test the hypothesis. This study has carried out to analysis the tax contribution of Merchant Bankers in the national receipts and problems relating to income tax payment. To achieve these stated objectives of this thesis a Research Method has been design in this thesis. The research method will contain research design, source of data collection, procedure of data collection, using tools and procedure of Data Presentation and Analysis.

3.1 Research Design

This thesis a type of descriptive design because the research entitled **"A study on Income Tax Collection from Merchant Bankers of Nepal"** has concerned with past phenomena both numerical as well as opinion. Thus, the study had followed the descriptive research design.

3.2 Data Collection Procedure

The data and information in this thesis report both were primary and secondary sources. All the numerical data had collected from the secondary sources while required information had collected from primary sources.

a. Primary sources: Primary data were collected through questionnaire circulation to the bankers as well tax authorities. Interview was done with the related parties during the field visit to get more information.

   In total 70 opinion questionnaire were distributed to different personnel. Among them, a total of 50(71.43%) filled questionnaire were received.

Among these 15(30%) were tax administrator, 15(30%) tax experts, 15(30%) taxpayers and 5(10%) were bank officials.

b. Secondary sources: Secondary data were obtained from various sources specified as follows:
   i. Annual report and published document of NRB.
   ii. Reports and records of department of taxation, Ministry of Finance HMG/Nepal.
   iii. Budget speech and Economic survey of varies of various years, (MOF) HMG/Nepal.
   iv. Books related to income tax and public finance.
   v. Annual reports of Merchant Bankers F.Y. 2002/03 to 2006/07.

3.3 Data presentation

Through collection of data and information from different sources, the data were tabulated and presented in table, charts and graphs to make analysis and interpretation easier.

3.4 Statistical tools used

Statistical tools used for making analysis and interpretation of collected data from different sources,

The tabulation, chart and diagrams were used along with simple percentage as demanded by subject matters.

From these tabulated data interpretations made by simple arithmetic mean and ratios wherever necessary.

Similarly, standard deviation and co-efficient of variation were used to show dispersion of tax paying from Merchant Banker.

CHAPTER – IV

PRESENTATION AND DATA ANALYSIS

This chapter deals with presentation and analysis of data related to income tax collection from merchant bankers. Under this selected merchant bankers are analyzed with used tables, graphs and line charts.

4.1 Structure of Nepalese Government Revenue

Government needs adequate budget for the development activities, operation of administration, maintaining peace and security and for other welfare activities. The required budget is collected from various sources. Generally, the revenue collected by the government from various sources is known as public revenue/public receipt/national revenue/National exchequer. The structure of the government revenue in Nepal is the composition of tax revenue and non-tax revenue. Tax revenue includes various direct taxes as well as indirect taxes. A direct tax includes income tax, property tax, house & building registration vehicle tax and others. An indirect tax includes customs, excise, value-added tax and other.

On the other hand, non tax revenue is the composition of various receipts from different government entities. The government revenue is therefore, the mix (combination) of tax revenue and non-tax revenue are consisting various sources. Mostly, income of the government is collecting from indirect tax in Nepal. They are custom duty, excise duty and sale tax or VAT. Custom duties consist of export, import, Indian excise refund and miscellaneous. The excise duty is the imposition of tax on liquor production, tobacco production and other industrial production. The other indirect taxes, which are also important in government in government revenue, are contract tax, hotel tax, entertainment tax and air flight tax.

Direct tax revenue includes Income tax, house & building registration, property tax, vehicle tax etc. The income tax is directly imposed upon the individuals' income or profit. Income tax is the composition of income or profit of public enterprises semipublic enterprises, private corporate bodies, individuals and remuneration. The house and land registration, property tax and vehicle tax is also the part of indirect tax.

Non tax revenue of the government includes various registration fees, income from sale of government services and products. Dividend received royalties, principal and interest received and miscellaneous. The registration fees include firm registration, vehicle registration, and license registration and so on. Water charge, electricity charge, telephone charge, post service, income from education, Income from food, agriculture and income from transportation are the major factors of sales of government services and products. Government receives dividends from financial institutions, trading companies, industrial enterprises and service-oriented organizations. Similarly, royalty from mine is also the non-tax revenue of the government.

The government revenue includes different items. They are indirect taxes, direct taxes and non-taxes. As shown in table 4.1 more than 75% has been collected from tax revenue in every year by the government. Government is collected revenue from total taxes in F.Y. 2002/03, 2003/04, 2004/05, 2005/06, 2006/07 was 75.74%, 77.29%, 77.16, 79.45 and 81.14 respectively. It showed was highly increasing trend. Tax revenue includes direct tax and indirect tax. Government is collected revenue from indirect taxes in F.Y. 2002/03, 2003/04, 2004/05, 2005/06, 2006/07 was 57.77%, 58.2%, 58.53%, 60.13% and 59.5% respectively. Though in F.Y. 2006/07 was collected in decreasing rate, it showed the increasing trend. In individual, value added tax showed increasing trend than others. It was collected

In F.Y. 2002/03, 2003/04, 2004/05, 2005/06, 2006/07 was 23.95%, 23.26%, 26.95%, 29.90% and 29.81% respectively.

Government collected revenue from direct taxes in F.Y. 2002/03, 2003/04, 2004/05, 2005/06, 2006/07 was 17.97%, 19.09%, 18.63%, 19.32% and 21.64% respectively. It showed slightly increase from F.Y. 2002/03 to 2003/04 and decreased in F.Y. 2004/05 than, again it increased regularly till F.Y. 2006/07. In individual, Income tax showed increasing trend than others. It was collected In F.Y. 2002/03, 2003/04, 2004/05, 2005/06, 2006/07 was 14.46%, 15.25%, 14.91%, 15.13% and 17.93% respectively.

Government collected revenue from Non- taxes in F.Y. 2002/03, 2003/04, 2004/05, 2005/06, 2006/07 was 24.26%, 22.71%, 22.84% 20.55% and 18.86% respectively. It showed highest revenue in F.Y. 2002/03 and lowest revenue in F.Y.2006/07. Hence, non-tax revenue contribution showed slightly up and down each year. In individual, duties & fees showed increasing trend than others. It was collected In F.Y. 2002/03, 2003/04, 2004/05, 2005/06, 2006/07 was 3.91%, 5.21%, 5.38%, 5.75% and 5.84% respectively.

Thus the tax revenue is the highest contributing source of total government revenue. But non tax revenue has also been contributing in considerable rate among the other individual revenue items. It has captured second and third position in the different F.Y. s when comparison is made among all revenue items individually. In conclusion, the composition of government revenue has different types of tax and non-tax revenue items. The income tax is in increasing order from the beginning of analysis and it to be progressive in future items. The income tax in increasing order from the begging of analysis and it is progressive in future. This is denoted by higher growth rate of this revenue item.

Table 4.1: Composition of Government Revenue in Nepal by Heads

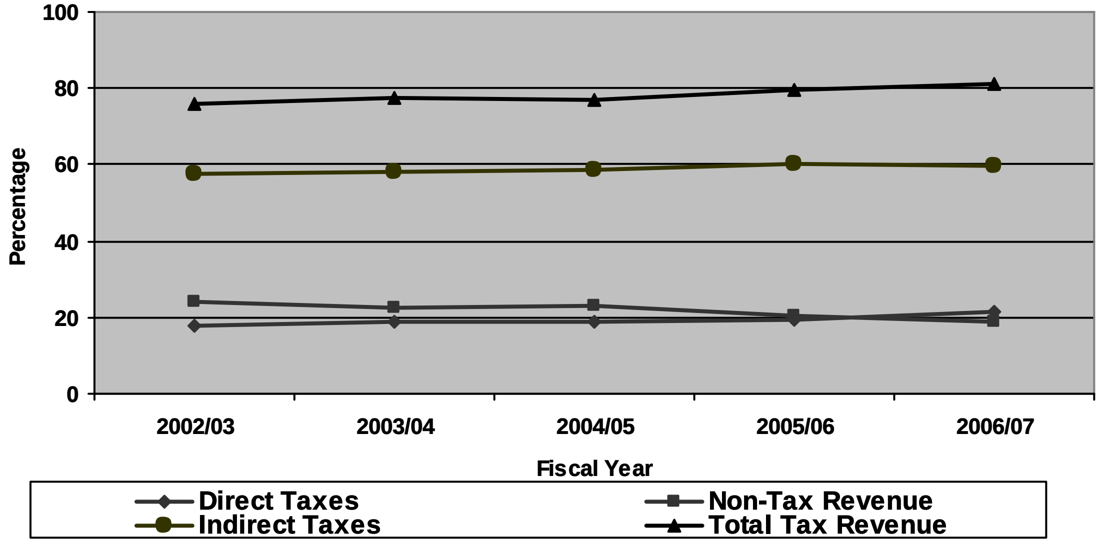
(Rs. in million)

F.Y.	2002/03		2003/04		2004/05		2005/06		2006/07	
Revenues	**Rs.**	**%**	**Rs.**	**%**	**Rs.**	**%**	**Rs.**	**%**	**Rs.**	**%**
1. INDIRECT TAXES :	**32481.2**	**57.8**	**36274**	**58.2**	**41043**	**58.5**	**43466**	**60.1**	**52188**	**59.5**
a. Customs	14236.4	25.32	15554	24.95	15702	22.39	15344	21.23	16699	19.04
b. Value added tax	13467.3	23.95	14498	23.26	18896	26.95	21615	29.9	26145	29.81
c. Excise	4777.5	8.5	6221.4	9.98	6446	9.19	6506.5	9	9343.6	10.65
2. DIRECT TAXES:	**10105.8**	**18**	**11902**	**19.09**	**13061**	**18.63**	**13961**	**19.3**	**18980**	**21.64**
I. Income Tax	8132.2	14.46	9504	15.25	10456	14.91	10934	15.13	15730	17.93
II. House & Building Registration	1414.2	2.52	1697.5	2.72	1799	2.57	2180.3	3.02	2238.7	2.55
III. Property Tax	0.1	0	0	0	0	0	0	0	0	0
IV. Vehicle Tax	559.3	0.99	700.4	1.12	806.1	1.15	847.6	1.17	1011	1.15
3. NON TAX REVENUE:	**13642.8**	**24.3**	**14155**	**22.71**	**16018**	**22.84**	**14855**	**20.6**	**16544**	**18.86**
i. Duties & Fees	2200.8	3.91	3245	5.21	3771	5.38	4153.8	5.75	5126.4	5.84
ii. Fines and Forfeiture	166.9	0.3	133.2	0.21	173.5	0.25	551.6	0.76	251.3	0.29
iii. Public Utilizes	1274.3	2.27	1321.3	2.12	1266	1.81	1150.7	1.59	1310.4	1.49
iv. Dividends	2497.6	4.44	2661.1	4.27	4590	6.55	3394.8	4.7	4937.7	5.63
v. Interest	924.6	1.64	1656.5	2.66	1467	2.09	1734.6	2.4	1049.8	1.2
v. Royalty and sales of government property	1945.4	3.46	1465	2.35	1932	2.75	1195.6	1.65	1095.7	1.25
vi. Principal Repayments	1539.7	2.74	1850.5	2.97	1248	1.78	1513.6	2.09	1025.6	1.17
vii. Miscellaneous Income	3093.5	5.5	1822.7	2.92	1571	2.24	1160.4	1.61	1747.2	1.99
A. Tax Revenue (1+2)	**42587**	**75.7**	**48176**	**77.3**	**54105**	**77.2**	**57427**	**79.5**	**71168**	**81.14**
B. Non Tax Revenue (3)	**13642.8**	**24.3**	**14155**	**22.7**	**16018**	**22.8**	**14855**	**20.6**	**16544**	**18.86**
TOTAL REVENUE (A+B)	**56229.8**	**100**	**62331**	**100**	**70123**	**100**	**72282**	**100**	**87712**	**100**

Sources : 1. Quarterly Economic Bulletin (2007) No. 3 NRB

2. Economic Survey (MOF)

Figure 4.1 Composition of Government Revenue in Nepal



4.2 Contribution of Tax Revenue to the Total Revenue

National exchequer is composition of tax revenue and non-tax revenue. Tax revenue has also direct and indirect taxes. Custom, excise duty, sales tax/VAT and other miscellaneous are the main revenue items of indirect tax revenue. Direct tax, however, is the composition of income tax, land tax, property tax, and other direct taxes. Non-tax revenue of the government is also important revenue source that includes different types of fees, charges, dividend, royalty and principle with interest from companies and corporations. Sale of fixed assets and mint are also components of non-tax revenue. Table 4.2 shows the comparison between tax revenue and non-tax revenue collection.

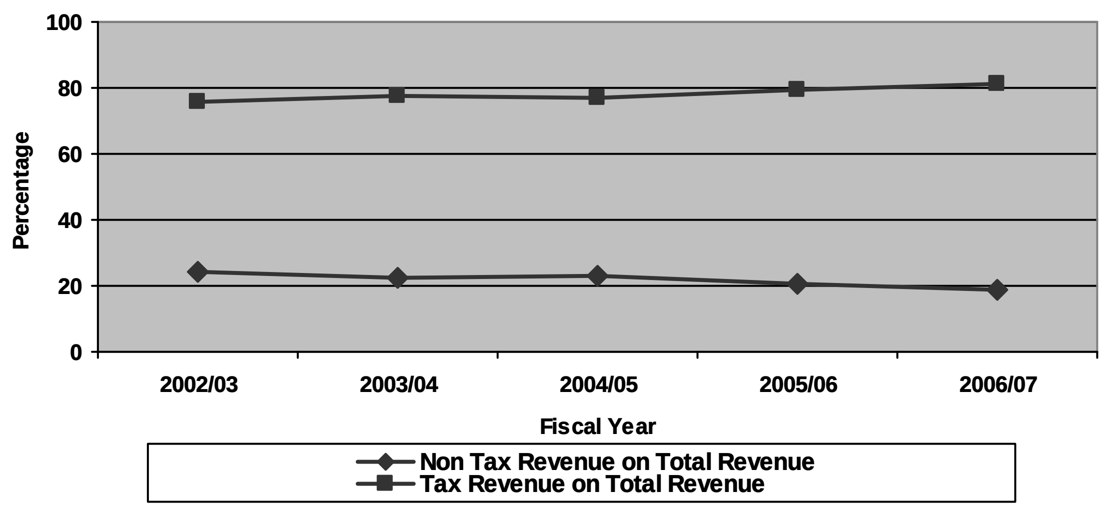
Table 4.2 Contribution of Tax Revenue/Non Tax revenue to the Total Revenue

(Rs. in million)

F.Y.	Total Revenue	Tax Revenue	%	Non-tax Revenue	%
2002/03	56229.8	42587	**75.74**	13642.8	**24.26**
2003/04	62331	48175.7	**77.29**	14155.3	**22.71**
2004/05	70122.6	54104.7	**77.16**	16017.9	**22.84**
2005/06	72282.1	57427	**79.45**	14855.1	**20.55**
2006/07	87712.1	71168	**81.14**	16544	**18.86**
Average collection			**78.15**		**21.85**

Sources : 1. Quarterly Economic Bulletin (2007) No. 3 NRB
2. Economic Survey (MOF)

Figure 4.2: Contribution of Tax Revenue/Non Tax Revenue to the Total Revenue



As shown in the table 4.2, tax revenue contributed more than 75% in the total revenue realization. In the F.Y. 2002/3, tax revenue contributed 75.74%, F.Y.

2006/07 showed the highest realization of tax revenue i.e. 81.14%. It shows regularly increased till F.Y. 2006/07. In the F.Y. 2002/3, non-tax revenue contributed highest revenue 24.26%, and F.Y. 2006/07 showed the lowest realization of tax revenue i.e. 18.86%. Non-tax revenue contribution showed slightly up and down each year. The above analytical company thus, shows that the tax revenue was contributing more than non-tax revenue. Tax revenue decreased to 75.74% the lowest in the F.Y. 2002/03. When non-tax revenue was realized 24.26% the highest realization rate in the same F.Y. This analysis also showed the average revenue collection through tax revenue and non-tax revenue (averaging for last five years). As shown by table, the average contribution of tax revenue was 78.15% where as the contribution made by non-tax revenue was 21.85%. This interpretation is also understood through the given figure no. 4.2 which visualizes the same matter.

4.3 Share of Direct Tax on Total Tax Revenue and Total Revenue

Tax Revenue is divided into two classes one is direct and other is indirect. A direct tax is such type of tax, which is imposed upon the person out of his income or property. A direct tax is really paid by the person on whom it is legally imposed. The taxpayer from other person cannot realize this type of tax. He must pay it from his own pocket. Income tax, property tax, expenditure tax, gift tax, death tax, contract tax, vehicle tax and others are the best examples of direct taxes. On the other hand, an indirect tax is such type of tax, which is imposed upon any person without direct collecting from him. An indirect tax is imposed on one person but paid partly or wholly by another. Sale tax/VAT, entertainment tax, customs, excise duty are the good examples of this tax. Thus direct tax is any tax which is imposed on a person who bears its economic impact by himself, indirect tax is any tax in which the economic impact is passed to other person for instance, government imposes value added tax on goods sold, but the amount of VAT is collected from customers. Here tax is imposed upon sales man. However, the buyer pays tax indirectly.

Table No. 4.3 shows the contribution ration of direct tax on tax revenue and total revenue of the government. This relationship is also presented in the figure no. 4.3. The initial share of direct tax on total revenue was 17.97% which was 23.73% on total revenue in the F.Y. 2002/03. In that year Rs.10105.8 million was collected from the direct tax. In F.Y. 2003/04 the share of direct tax on total revenue was 19.09% and 24.71% on total tax revenue. In F.Y. 2004/05 it decreased 18.63% and 24.14% respectively. Then after it started to increase till 2006/07 was 21.64% and 26.67 % respectively.

Table 4.3: Ratio of Direct Tax in Total Tax Revenue and Total Revenue

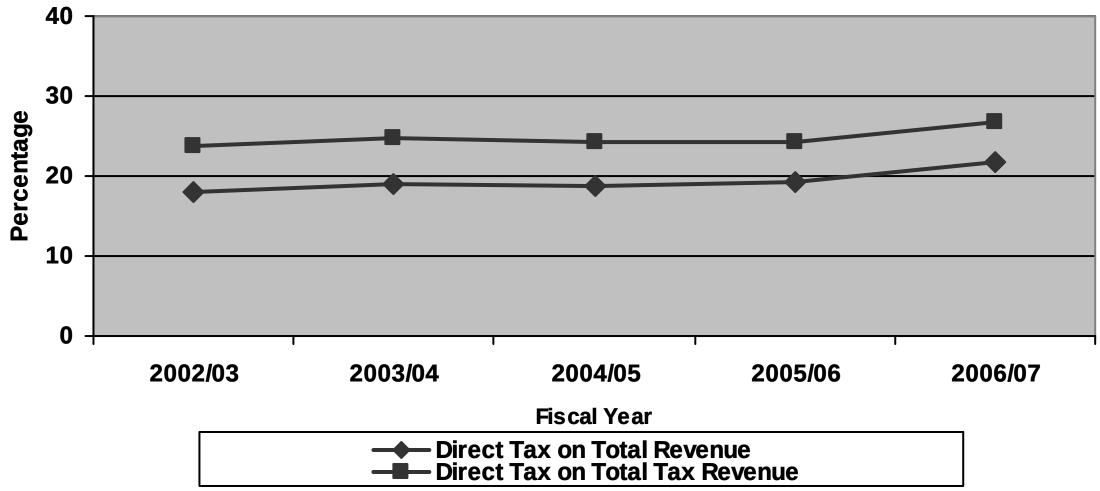
(Rs. in million)

F.Y.	Total Revenue	Total Tax Revenue	Direct Tax	Direct Tax on Total Revenue	Direct Tax On Total Tax Revenue
2002/03	56229.8	42587	10105.8	**17.97**	**23.73**
2003/04	62331	48175.7	11901.9	**19.09**	**24.71**
2004/05	70122.6	54104.7	13061.3	**18.63**	**24.14**
2005/06	72282.1	57427	13961.4	**19.32**	**24.31**
2006/07	87712.1	71168	18979.7	**21.64**	**26.67**

Sources : 1. Quarterly Economic Bulletin (2007) No. 3 NRB

2. Economic Survey (MOF)

Figure 4.3: Ratio of Direct Tax in Total Tax Revenue and Total Revenue



Direct Tax on Total Revenue is more fluctuating than Direct Tax on Total Tax Revenue. The reason behind of fluctuating was highest tax collection from indirect tax. The income tax collection has been increasing due to increasing number of taxpayer and their taxable revenue and profit. In conclusion, it can be said that the positive trend of direct tax denoted economic improvement of the nation, even though the nation is in deep trouble in these days due to the political crisis.

4.4 Structure of Income Tax in Nepal

Income tax is levied on net taxable income. This means that not all incomes accrued from sources brought in to the income pay income tax. Both are persons as mentioned by income tax Act, 2002. The tax levied upon individual is known as personal income tax whereas income tax levied upon individual known as personal income tax whereas income tax levied to organization is called corporate tax. The government therefore income tax upon the person (individuals, firms and companies) earning taxable incomes, without direct benefit to them.

Income Ta Act, 2002 has clearly defined the related terms. It has defined the tax head for computation of tax liabilities. According to this law, three income headings including various receipts are mentioned as follows:

I. Income from Business: This head of income includes income and profit from industry, business, profession and from other business transactions, professional fees, service fees, sales proceeds of business stocks, amount received from disposal business assets and liabilities, proceeds from disposal of depreciable assets, business gifts, receipts from business restriction and receipts of amount from directly related to business.

II. Income from Employment: This head of income includes various receipts. They are wages, salaries, allowances, fees, commission award, gift, bonus and other facilities. The other facilities include additional payment for Dashain, housing facility, vehicle facility and telephone facility and so on. Similarly dearness allowance, house rent. Entertainment, transportation and cost of living expenses are also the remuneration incomes of employees. Besides these, receipts made in agreement of doing job and any receipts in retirement such as retirement contribution and other amount prescribed by income tax act are the subject to tax.

III. Income from Investment: The third head of income is investment income, which includes various incomes received by investing assets in any business sector. They are divided, interest, rent receipts, receipts from investment insurance, gain from unrecognized retirement fund. It also includes proceeds from sale of non-business assets. Capital gains from disposal of depreciable assets, gifts received in relation with investment, amount received in the acceptance of restriction of investment and others. Thus, taxable income is composition of above mentioned various income sources. Income tax is divided into two types in broad sense viz. personal income tax and corporate income tax. Both have different income sources. Corporate tax is a composition of three taxpayers. They are government enterprises, public limited company and private limited company.

Individual income tax includes income tax from remuneration, industries, trade and profession of individual. Besides these, rent and interest taxes are also include in income tax. This is shown in table no, 4.4. The trend of income tax realization is shown in table 4.4 for the last five years. According to the table the total income tax realized in F.Y. 2002/03, 2003/4, 2004/05 2005/06/ 2006/07 was Rs.8132.2, Rs.9504, Rs.10456, Rs.10933.6, Rs.15730 million respectively. In table 4.4 there are mainly four components of sources on income tax. They are as follows: A. Corporate income tax, B. Remuneration income, C. Investment income, D. other taxes. Sources of corporate income tax are mixed by Government Corporation, Public Ltd. Corporation, Private Ltd. Corporation, Individual & sole trading firm and Income from other institutions. The highest income tax collection in F.Y. 2002/03 by individual & sole trading firm, F.Y. 2003/04 by government corporation, F.Y.2004/05 to F.Y. 2006/07 by public Ltd corporation was 22.16%,, 21.64%, 23.60%, 31.15% and 36.64%. These all incomes are the sources of corporate income tax.

The contribution of corporate income tax was in F.Y. 2002/03 by 68.30% where remuneration income, investment income and other taxes were 15.36%, 16.25%, 0.09% respectively in same year. In F.Y. 2003/04 the contribution of corporate income tax was by 71.6% where remuneration income, investment income and other taxes were 14.66%, 13.59%, 0.15% respectively in same year. In F.Y. 2004/05 the contribution of corporate income tax was by 70.12% where remuneration income, investment income and other taxes were 16.05%, 13.64%, 0.20% respectively in same year. In F.Y. 2005/06 the contribution of corporate income tax was by 69.30% where remuneration income, investment income and other taxes were 16.20%, 14.15%, 0.36% respectively in same year. In F.Y. 2006/07 the contribution of corporate income tax was by 73.78% where remuneration income, investment income and other taxes were 12.76%, 13.22%, 0.24% respectively in same year. Hence corporate income tax is main sources of government revenue.

Table 4.4: Structure of income tax revenue in Nepal

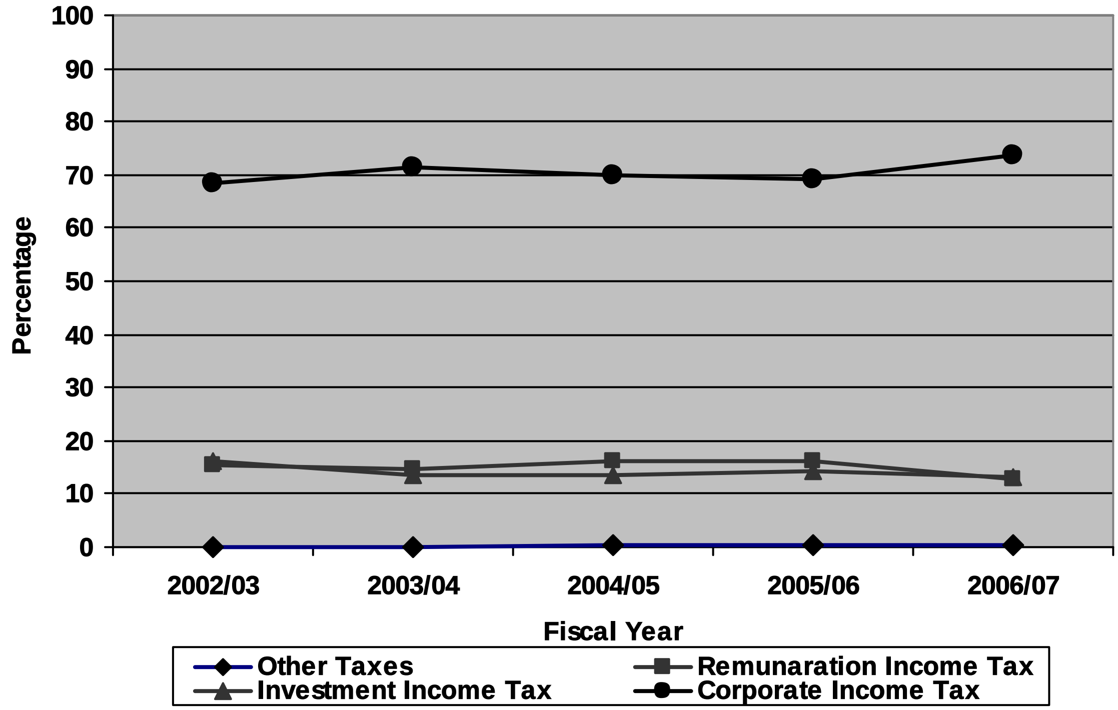
(Rs. in million)

F.Y. / Particulars	2002/03 Rs.	%	2003/04 Rs.	%	2004/05 Rs.	%	2005/06 Rs.	%	2006/07 Rs.	%
A. Corporate Income Tax :	**5554.0**	**68.3**	**6805.0**	**71.6**	**7331.3**	**70.1**	**7576.6**	**69.3**	**11605.0**	**73.78**
i. Government Corporation	1251.0	15.38	2056.60	21.64	1331.5	12.73	195.8	1.79	1019.5	6.48
ii. Public Ltd. Corporation	1235.1	15.19	1531.30	16.11	2467.6	23.60	3405.6	31.15	5716.4	36.34
iii. Private Ltd. Corporation	1166.7	14.35	1239.80	13.05	1527.3	14.61	1703.0	15.58	2310.0	14.69
iv. Individual & sole trading firm	1801.7	22.16	1869.70	19.67	1876.8	17.95	1958.8	17.92	2303.4	14.64
v. Income from other institutions	99.5	1.22	107.60	1.13	128.1	1.23	313.4	2.87	255.6	1.62
B. Remuneration Income:	1249.0	**15.36**	1392.90	**14.66**	1678.2	**16.05**	1771.1	**16.20**	2006.8	**12.76**
C. Investment income:	1321.5	**16.25**	1291.9	**13.59**	1425.9	**13.64**	1546.6	**14.15**	2080.1	**13.22**
D. Other taxes	7.7	**0.09**	14.2	**0.15**	20.6	**0.20**	39.3	**0.36**	38.2	**0.24**
INCOME TAX (A+B+C+D)	**8132.2**	**100**	**9504.0**	**100**	**10456.0**	**100**	**10933.6**	**100**	**15730.0**	**100.00**
GROWTH RATE	**-9.49**		**14.43**		**9.10**		**4.37**		**30.49**	

$$\text{Growth rate} = \frac{\text{Current Year's Collection} - \text{Previous Year's Collection}}{\text{Current Year's Collection}} \times 100$$

Source: Economic Bulletin, (2007) NRB

Figure 4.4: Income Tax Structure



4.5 Role of Corporate Tax in Nepal

Corporate tax, a part of total income tax, is also very important in the developing countries. Nepal is a poor and land locked countries. It has deficit budget from the very beginning of budgeting practice. It also needs to execute many development programs in the country. Unfortunately, the whole economic sector of Nepal has been badly affected due to various reasons, such as poor education system, least development of infrastructure, poor trade relationship with third countries of the world, lack of strong commitment of the government, instability of government and politics and so on. Income tax is one of the best and vital resources of national revenue that can be mobilized in the country to get national development. It is only justifiable to increase for the internal resource mobilization due to its nature. Increment of other tax rates make heavy burden to people because all the indirect taxes are shifted to the customers indirectly. It affects serous economic problems in the development countries like Nepal. But income tax rate can be increased because it is levied to the income generator without affecting other persons. It makes incentives to the people to work hard and increase economic transactions. Number of taxpayers can also be increased by investigation of potential taxpayers who are hidden.

The income taxes have positive effect on ability to work will be more than compensated by government's expenditure on the poor and middle class to rise their levels of income to raise levels of consumption and to provide them with better housing and better education. Income tax is levied not only for raising national revenue but also for making balance between the rich and poor people. In other words, it attempts to reduce inequalities that arise because of property. A highly progressive income tax, if administered property, should be able to reduce inequalities in short run. Income taxes are steeply progressive exempting low incomes taking only a small percentage out of small income and falling heavily on incomes running into lakes and corers. Most of countries, thus, have been extensively used income taxes not only for the revenue they bring to the state but also to solve the problem of inequality of incomes. More over, the government itself will be one of the main sources of capital formation as it will invest part of the tax proceeds in industries, transport and communication etc. Thus if the revenue from income taxes will be devoted to nation building to stabilize and promote business activity and thus increase the volume of national income.

Corporate tax, a part of total income tax, is also very important in the developing countries. People of such countries are not capable to pay individual income tax due to being less income earners. In this situation income tax from corporate bodies plays vital role in resource mobilization in the nation, if there are more industries are in operating. The other positive points of corporate tax are that they are easily identifiable and keep accounts in proper way. The do not escape from tax liability and practice tax evasion that is done by individual taxpayers. But unfortunately, Nepal is not able to increase industries in the country. Some government enterprises are privatized. Out of them, most are not in operation and private Ltd. May practice of tax evasion. This makes less realization of corporate tax to the government. As said earlier, there are only limited numbers of corporate bodies in the country. Their economic performance is also very low. Because of treasury is not much satisfactory in Nepal even through its contribution ratio is high in total income in Nepal.

Table 4.5 shows the contribution of corporate tax on total income tax with its growth rate during F.Y. 2002/03 to 2006/07. About Rs.5554 million has realized in the F.Y. 2002/03m which was 68.30% of total income tax collection. It was continuously rise to Rs.6805 million in the F.Y. 2003/04 with of contribution to total income tax i.e. 71.60%. After F.Y. 2003/04 the amount realized from corporate tax and total income tax declined to F.Y. 2005/06 where contribution of corporate tax on total income tax in F.Y. 2004/05 and F.Y. 2005/06 were 70.12% and 69.30% respectively. Than after it increased in F.Y.2006/07 by 73.78%. In F.Y. 2002/03 to 2006/07 growth rate showed (30.58%), 18.38%, 7.18%, 3.24% and 34.71%. In the F.Y. 2002/03 the growth rate was negative hence growth rate is very fluctuating trend within five years.

Table 4.5: Contribution of corporate Tax in Total Income Tax Revenue

(Rs. In million)

F.Y.	Total Income Tax	Corporate tax	% on TIT	Growth Rate
2002/03	8132.2	5554.0	**68.30**	**-30.58**
2003/04	9504.0	6805.0	**71.60**	**18.38**
2004/05	10456.0	7331.3	**70.12**	**7.18**
2005/06	10933.6	7576.6	**69.30**	**3.24**
2006/07	15730.0	11605	**73.8**	**34.71**

Source : 1. Quarterly Economic bulletin, 2007

2. Economic Survey, 2003/04 and 2006/07

3. Annual Report of IRD 2006/07

Figure 4.5: Contribution of corporate Tax in Total Income Tax Revenue with Growth rate

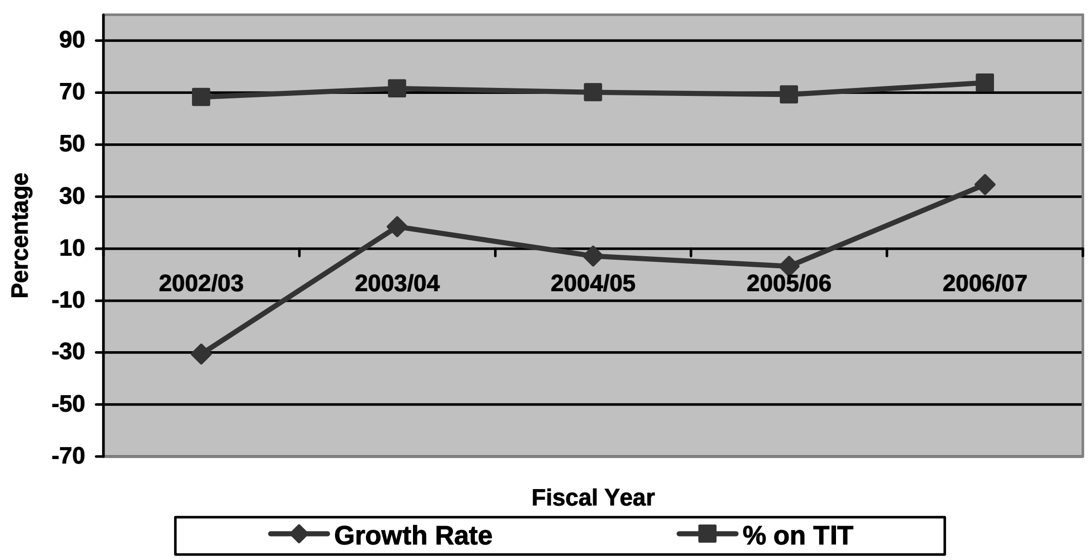


Table 4.6: Contribution of Corporate Tax on Government Revenue

(Rs. in million)

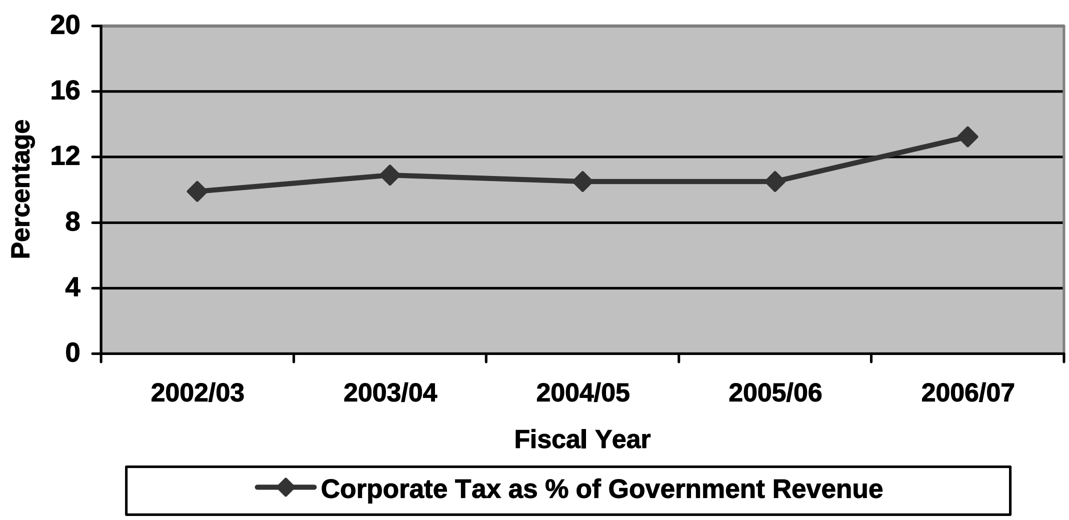
F.Y.	Govt. Revenue	Corporate Tax	Corporate Tax as % of G.R.
2002/03	56229.8	5554.0	9.9
2003/04	62331.0	6805.0	10.9
2004/05	70122.6	7331.3	10.5
2005/06	72282.1	7576.6	10.5
2006/07	87712.1	11605	13.23

Source : 1. Quartely Economic Bulletin (2007) No…NRB

2. Economic Survey 2003/04 and 2006/07

3. Annual Report of IRD, 2006/07

Figure 4.6: Contribution of Corporate Tax as percentage of government revenue



Corporate income tax is the direct tax which is the main sources of Government revenue. Table 4.6 shows the contribution of corporate tax on Government Revenue. In F.Y. 2002/03 corporate tax contributed to government revenue by 9.9% which was 10.9% in F.Y. 2003/04. In F.Y. 2004/05 to 2005/06 contributed by same ration i.e. 10.5% than after it increased in F.Y. 2006/07 was 13.23%.

Table 4.7: Corporate Tax/Income Tax Collection from Listed Merchant Bankers

(Rs. In Million)

S.N.	Particular	2002/03	2003/04	2004/05	2005/06	2006/07	Total
1	NMB Bank Ltd.	11.76	16.79	11.50	38.07	34.65	**112.77**
2	Nepal Housing and Merchant Finance Ltd.	1.56	2.10	7.94	10.04	13.30	**34.94**
3	Development Credit Bank Ltd.	12.58	12.02	19.56	21.10	25.79	**91.04**
4	Citizen Investment Trust	2.51	4.89	5.86	8.89	9.47	**31.61**
5	Nepal Finance Limited	2.93	9.62	6.06	7.03	12.71	**38.34**
6	Nepal Share Markets Finance Company Ltd.	1.80	2.01	12.07	13.41	16.85	**46.13**
7	NIDC Capital Markets Ltd.	-	15.21	17.02	26.19	25.97	**84.39**
	Total	**33.14**	**62.64**	**79.99**	**124.73**	**138.73**	**439.22**

Source : Annual Report of Relevant Merchant Banker (2002/03 to 2006/07)
Note : Tax Amount paid from cash flow statement.

Table 4.8: Average Corporate Tax Collection from Listed Merchant Banker.

(Rs. In Million)

S.N.	Particular	Mean Payment of of Corporate Tax	Standard Deviation of Payment	Coefficient of variation
1	NMB Bank Ltd.	22.55	11.48	0.51
2	Nepal Housing and Merchant Finance Ltd.	6.99	4.55	0.65
3	Development Credit Bank Ltd.	18.21	5.25	0.29
4	Citizen Investment Trust	6.32	2.58	0.41
5	Nepal Finance Limited	7.67	3.31	0.43
6	Nepal Share Markets Finance Company Ltd.	9.23	6.18	0.67
7	NIDC Capital Markets Ltd.	16.88	9.56	0.57

Source: Appendix-II of this Report

Table 4.8, shows the average corporate tax payments made by Merchant Bankers with standard deviation and coefficient of variation of tax payment. As shown by this table NMB Bank Ltd., Development Credit Bank Ltd. And NIDC Capital Markets Ltd. are the top three corporate taxpayer out of these seven Merchant Bankers. The Coefficient of variation demonstrates the variation of paying of corporate tax from the central tendency i.e. mean payment. As per the same table, the Development Credit Bank Ltd., has less C.V. i.e. 0.29 percentage. It means that its corporate tax paying was very close to the average payment than others. Nepal Share markets Finance Company Ltd. has highest C.V. That is why it has high volatile in income tax paying.

Table 4.9: Contribution Ratio of Income Tax paid by Merchant Bankers to Total Government Revenue & Total Tax Revenue

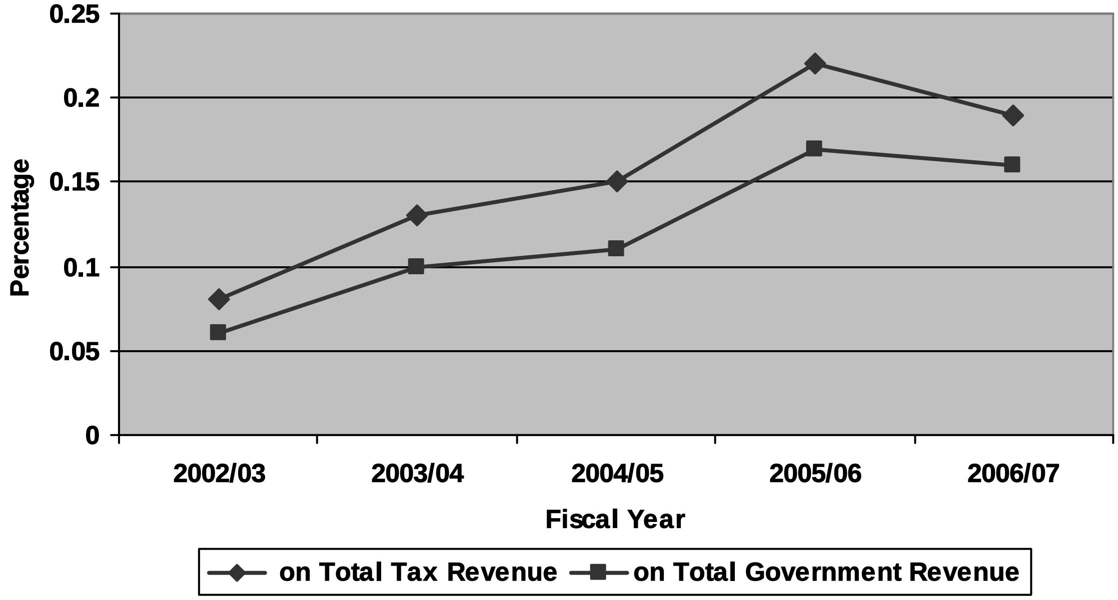
(Rs. In Million)

F.Y.	Total Govt. Revenue	% on Total Govt. Revenue	Corporate Tax Collected From Merchant Banker	Total Tax Revenue	% on Total Tax Revenue
2002/03	56229.8	0.06	33.14	42587	0.08
2003/04	62331	0.10	62.64	48175.7	0.13
2004/05	70122.6	0.11	79.99	54104.7	0.15
2005/06	72282.1	0.17	124.73	57427	0.22
2006/07	87712.1	0.16	138.73	71168	0.19

Source :

1. Economic Survey 2003/04 and 2006/07
2. Annual Report of Merchant Banker 2002/03 to 2006/07

Figure 4.7: Contribution Ratio of Income Tax paid by Merchant Bankers to Total Government Revenue & Total Tax Revenue



The Table 4.9: and Figure 4.7: presents the contribution ratio of corporate tax collected from listed merchant bankers in total tax revenue and in total government revenue for the last five years. According to the table, the contribution of corporate tax collected from merchant bankers in the F.Y. 2002/03 about Rs.33.14 million, which contributed 0.06% in the total government revenue. In the same year, its contribution on total tax revenue was 0.08%. In the last year F.Y. 2006/07, the realization of tax from listed merchant bankers were 138.73 million, which contributed 0.16% to total government revenue and 0.17% to total tax revenue. From the same table it can be said that the contribution of tax payment made by the listed merchant bankers is in increasing trend till F/Y 2005/06 but slightly decreased in F/Y 2006/07 as compared to F/Y 2005/06. Table has showed slightly increasing trend, however it is not satisfactory situation. The reason behind this situation was bad political condition, instability and conflict which directly hampered the other economic sectors.

Table 4.10: Contribution Ratio of Income Tax Collection from Merchant Banker to Total Income Tax and Corporate Tax

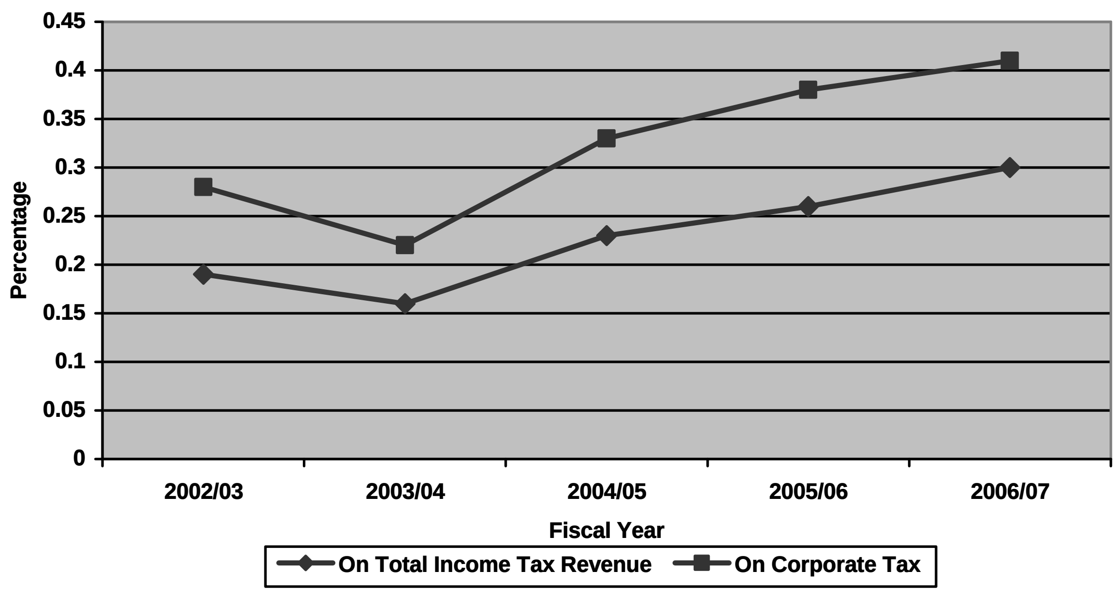
(Rs. In million)

F.Y.	TIT Revenue	% on TIT	Corporate Tax Collection from listed M. B.	Corporate Tax	% on Corporate Tax
2002/03	8132.2	0.41	33.14	5554	0.60
2003/04	9504	0.66	62.64	6805	0.92
2004/05	10456	0.77	79.99	7331.3	1.09
2005/06	10933.6	1.14	124.73	7576.6	1.65
2006/07	15730	0.88	138.73	11605	1.20

Sources:

1. Annual report of IRD, 2006/07
2. Annual Report of Merchant Banker, 2002/03 to 2006/07.

Figure 4.8: Contribution Ratio of Income Tax Collection from Merchant Bankers to Total Income Tax and Corporate Tax



This part of analysis represents by table 4.10: and figure 4.8: According to this table and chart, the contribution of corporate tax collected from listed merchant bankers were 0.41% and 0.60% in the F.Y. 2002/03 in total income tax and total corporate tax realized by the government respectively. In the year about Rs.33.14 million was collected as corporate tax from listed merchant bankers. In F.Y. 2006/07 corporate tax collected from listed merchant bankers were decreased to 0.88% and 1.20% as compared to that of F/Y 2005/6 which were 1.14 and 1.65 in total income tax and total corporate tax realized by the government respectively. Except to F/Y 2006/07 to all the years collection amount is in increasing trend.

Table 4.11 Relationship of Corporate Tax and Tax Collected from Listed Merchant Bankers with Gross Domestic Product

The Corporate tax and tax collection from listed Merchant Bankers to GDP are shown in table 4.11. Gross domestic product (GDP) means the value of goods and services produced within the nation. If it is represented in the income of the factors of production, it is known as GDP at factor cost whereas it is known as GDP at market price if goods and services are charged at ruling prices. Prices include all taxes on expenditure subsides being regarded as negative taxes. For the analysis, gross domestic produce at current market prices is taken as base. As shown by the table 4.11, the contribution ration of these two taxes has been very low in GDP even though both have been increasing.

(Rs. In Million)

F.Y.	Gross Domestic Product (GDP)	Growth Rate (GDP)	Corporate Tax	Corporate Tax Collection from listed M.B.	Corporate Tax as % of GDP	Corporate Tax from Listed M.B. as % of GDP
2002/03	438920	7.85	5554	33.14	1.27	0.01
2003/04	474242	7.45	6805	62.64	1.43	0.01
2004/05	589412	19.54	7331.3	79.99	1.24	0.01
2005/06	646471	8.83	7576.6	124.73	1.17	0.02
2006/07	719477	10.15	11605	138.73	1.61	0.02

Source: 1. Economic Survey, 2003/04 and 2006/07

2. Annual reports of IRD, 2006/07
3. Annual reports of merchant banker 2001/02 to 2006/07

In the F.Y. 2002/03 the GDP growth rate was 7.85% where GDP was Rs.438920 million. The share of corporate tax and corporate tax collection from listed merchant bankers to the GDP were 1.27% and 0.01% respectively in same year. The GDP growth rate down to 7.45% in the F.Y. 2003/04 and the share of corporate tax to the GDP increased to 1.43%, where corporate tax collection from listed merchant bankers to the GDP is same as that of F/Y 2002. In F.Y. 2005/06 to F.Y. 2006/07 showed same ratio i.e. 0.02% in corporate tax collection from listed merchant bankers to the GDP, where the share of corporate tax to the GDP was 1.17% and 1.61% respectively.

4.6 Empirical investigation

An empirical investigation has been conducted to find out different aspect of Nepalese income tax and public enterprises income tax imposition in Nepal. The major tool used in survey research was an opinion questionnaire was distributed to 70 persons. The questionnaire included the various aspects of income tax concerning with selected Merchant Bankers and IRD. A total of 50(71.43%) filled questionnaire were received. Among these 15(30%) were tax administrator, 15(30%) tax experts, 15(30%) taxpayers and 5(10%) were bank officials.

The respondent were asked either to response yes/no or tick best answer one or to write their opinion. Some of the respondents have chosen more than one answer and ranked them respectively. Information received from all of respondents was tabulated in to the separate table format and they were presented in percentage of total numbers or point then analyzed in to a descriptive way. The respondents were selected four denominations and code was used to represent each denomination in order to make easy the analysis. The following table shows denomination of respondents and code used to represent them.

Table 4.12: Denomination of Respondents and Code

S.N.	Denomination of Respondents	Code used
1.	Income Tax Administrator	A
2.	Income Tax Exports	E
3.	Income Tax Payer	P
4.	Bank officials	O

4.6.1 Income tax as a suitable means of raising domestic resources

In order to know whether income tax as suitable means of raising domestic resources, a question was asked, “In your opinion, is the income tax as a suitable means of raising domestic resources in Nepal? The respondents received from respondents are tabulated as follows.

Table 4.13: Income tax as a suitable means of raising domestic resources

Response / Respondents	A	E	P	O	Total	Percentage
Yes	17	17	7	7	48	96
No	0	0	2	0	2	4
Total	17	17	9	7	50	100

Source: Opinion Survey

The question was received from all respondents 96% of total respondents accept the income tax, as a suitable means of domestic resource and only 4% of total respondents does not recognize income tax a suitable means of domestic resources mobilization. Thus the conclusion can be drawn than the income tax is suitable means of raising government revenue.

As the corollary to the earlier question a question was asked, “If yes, why it is a suitable means for raising domestic resources? The opinion respondents are presented in the following table.

Table 4.14: Reasons for Income Tax is a Suitable Means for Raising Domestic Resources

S.N.	Problems	Points	%	Rank
1.	It is harmful to depend fully on external sources	170	36	1
2.	Among the internal sources, taxation seems to be the most viable method	140	30	2
3.	It is not possible to cut the consumption level of people, as it is already too low	65	14	3
4.	Several limitations of public borrowings	57	12	4
5.	Others	35	8	5
	Total	467	100	

Source: Opinion Survey

From the above table it shows that harmful to depend fully on external sources are the main causes for income tax is a suitable means for raising domestic resources of Nepal. The reason for income tax is a suitable means for raising domestic resources are ranked below in order of preference.

- It is harmful to depend fully on external sources.
- Among the internal source, taxation seems to be the most viable method.
- It is not possible to cut the consumption level of people,as it is already too low.
- Several limitations of public borrowings.
- Others.

4.6.2 Soundness and Effectiveness if Income Tax System of Nepal

The most effective part of income tax system is its effectiveness and soundness. The question "Do you think the income tax system of Nepal is sound and efficient?" was asked. The responses are tabulated as follows.

Table 4.15: Soundness and Effectiveness of Income Tax System of Nepal

Response / Respondents	A	E	P	Total	Percentage
Yes	10	4	3	17	34
No	6	11	16	33	66
Total	16	15	19	50	100

Source: Opinion Survey

There was 100% response received from the respondents. Majority of the respondents disagree with sound and effectiveness of income tax system of Nepal. 66% of total respondents are unsatisfied. Only 34% are satisfied with the sound & effectiveness of income tax system of Nepal.

As the corollary to the earlier question a question was asked, "If no, what is the major problem of income tax, system of Nepal?" the opinion of respondents are presented in the following table.

Table 4.16: Major Problem of Soundness and Effectiveness of Income Tax System of Nepal

S.N.	Problems	Points	%	Rank
1.	Complexity in income tax policy, rules and regulation	115	24	2
2.	Inadequate government economic policy	125	26	1
3.	Lack of appropriate assessment procedure	100	21	3
4.	Lack of honest, trained and competent tax personnel	77	16	4
5.	Others	60	13	5
	Total	477	100	

Sources: Opinion survey

From the above table it is that inadequate government economic policy is the main cause for unsatisfactory of soundness and effectiveness of income tax system of Nepal. The reason for unsatisfactory of soundness and effectiveness of income tax system are ranked below in order of preference.

1. Inadequate government economy policy
2. Complex city in income tax policy, rules and regulation
3. Lack of appropriate assessment procedure
4. Lack of hones, trained and competent tax personnel
5. Others

4.6.3 Satisfaction towards Corporate Tax Rate in Nepal

Corporate tax rate plays a vital role in income tax. It is clear that the corporate tax rate should be such which enables the government to collect more amounts for its revenue and provide incentives to invest corporate sector. Exciting corporate tax rate in Nepal 25% whereas, in the financial corporate sector it is 30% tax rate. In order to find out the appropriate corporate tax at present is satisfactory or not. The responses of the respondents are as follows:

Table 4.17: Satisfaction towards Corporate Tax

Response / Respondents	A	E	P	O	Total	Percentage
Yes	15	15	15	5	50	
No	-	-	-	-	-	
Total	15	15	15	5	50	100

Source: Opinion Survey

There is 100% response received. The responses of respondents clear that the existing corporate tax rate i.e. 25% is satisfactory and do not need for change.

Thus the conclusion can be drawn out that the corporate tax rate that is 25% is appropriate.

4.6.4 Specific goal of Income Tax

Income tax is imposed on person's income in order to achieve some specific goal. As regards the specific goal of income taxation in Nepal, respondents were requested to rank their response on 1 (most important) to 4 lists important. The question was "what should be the specific goal of income tax in Nepal?" Below the table gives the breakdown of response.

Table 4.18: Specific Goal of Income Taxation in Nepal

S.N.	Goals of income tax	Group			Total points	%	Rank
		A	E	P			
1.	Increase the revenue of government	70	75	79	224	40	1
2.	Reduce the gap between poor and rich	50	45	55	150	27	2
3.	Promote private sector investment	42	37	35	114	21	3
4.	Reduce in unemployment	15	27	27	69	12	4
				Total	557	100	

Source: Opinion Survey

The specific goals of income taxation in Nepal are ranked in order of the percentage of the respondents and are as follows:

1. Increase the revenue of government.
2. Reduce the gap between poor and rich.
3. Promote private sector investment.
4. Reduce in unemployment.

Minimize tax avoidance & tax evasion, attract foreign business group and increase the feeling of social justice are some of the other goals as stated by the respondents.

From the above analysis it is clear that increase the revenue of government is the most important goal of income taxation in Nepal. It is also an important factor to reduce the gap between poor and rich.

4.6.5 Delay in Tax Assessment

A question was asked, "Do you accept that you make delay in tax assessment?" The responses received from respondents are tabulated as follows:

Table 4.19: Delay in tax assessment

Responses / Respondents	A	E	P	O	Total	Percentage
Yes	17	17	7	4	45	90
No	0	0	5	0	5	10
Total	17	17	12	4	50	100

Source: Opinion Survey

The question was received from all respondents 90% of total respondents accept the delay in tax assessment and only 10% of total respondents do not recognize delay in tax assessment. Thus the conclusion can be drawn than accept the delay in tax assessment.

As the corollary to the earlier question a question was asked, "If yes, what may be the reasons? The opinion respondents are presented in the following table.

Table 4.20: Reasons for Delay in Tax Assessment

S.N.	Problems	Points	%	Rank
1.	Delay in filing returns	167	36	1

2.	The assessment procedure itself takes long time	115	25	2
3.	Inefficiency of tax authorities	90	19	3
4.	Negligence of tax personnel	57	12	4
5.	Others	36	8	5
	Total	465	100	

Source: Opinion Survey

From the above table it shows that delays in filing returns is the main cause for income tax is a delay in tax assessment. The reasons for delays in tax assessment are ranked below on order of preference.

1. Delays in filing returns.
2. The assessment procedure itself takes long time.
3. Inefficiency of tax authorities.
4. Negligence of tax personnel.
5. Others (please specify)

4.6.6 Types of complain do Merchant Bankers make

A question was asked, “What types of complains do Merchant Bankers make?” The respondents received from respondents are tabulated as follows.

Table 4.21: Types of Complain do Merchant Bankers make

S.N.	Problems	Points	%	Rank
1.	About tax assessment	217	40	1
2.	About behaviors of tax personnel	113	21	2
3.	About tax incentives	95	18	3
4.	About provisions included in income tax law	64	12	4
5.	About fines & penalties	40	7	5
6.	Others	9	2	6
	Total	538	100	

Source: Opinion Survey

The types of complain do Merchant Bankers make are ranked in order in order of the percentage of the respondents and are as follows:

1. About tax assessment.
2. About behaviors of tax personnel.
3. About tax incentives.
4. About provisions included in income tax law.
5. About fines and penalties.
6. Others

4.6.7 Filing Appeals by Merchant Bankers to Revenue Tribunal

A question was asked, "What may be the reasons for filing appeals by Merchant Bankers To Revenue Tribunal?" The responses received from respondents are tabulated as follows.

Table 4.22: Filing Appeals by Merchant Bankers to Revenue Tribunal

S.N.	Problems	Points	%	Rank
1.	Order of tax assessment by tax authorities	171	36	1
2.	Tax evasion	115	24	2
3.	Vague provision of tax law	99	21	3
4.	Use of discretion by tax authorities	50	11	4
5.	Others	35	8	5
	Total	470	100	

Source: Opinion Survey

The reasons for filing appeals by Merchant Bankers to Revenue Tribunal are ranked in order of the percentage of the respondents are as follows:

1. Order of tax assessment by tax authorities.
2. Tax evasion.
3. Vague provisions of tax law.
4. Use of discretion by tax authorities.
5. Others

4.6.8 The concession facilities and incentives to be given to the Merchant Bankers

A question was asked, "What types of tax concession facilities and incentive to be given to the Merchant Bankers?" The responses received from respondents are tabulated as follows.

Table 4.23: Tax concession facilities and incentives to be given to the Merchant Bankers

S.N.	Problems	Points	%	Rank
1.	Tax holiday	209	38	1
2.	Investment Credit	107	19	2
3.	Carry forward of losses	95	17	3
4.	Tax rate deduction	71	13	4
5.	Accelerated depreciation	45	8	5
6.	Others	25	5	6
	Total	552	100	

Source: Opinion Survey

The types of tax concession facilities and incentives to be given Merchant Bankers are ranked in order of the percentage of the respondents and are as follows:

1. Tax holiday.
2. Investment credit.

3. Carry forward of losses.
4. Tax rate deduction.
5. Accelerated depreciation.
6. Others

4.6.9: Effectiveness of tax administration to impose fine and penalties

In order to know the effectiveness of tax administration to impose fines and penalties in Nepal, a question was asked, “Do you think the tax administration of Nepal is effective to impose fines and penalties as per necessary? The following table shows:

Table 4.24: Effectiveness of tax administration to impose fines & penalties

Response / Respondents	A	E	P	Total	Percentage
Yes	5	12	0	17	38%
No	10	3	15	28	62%
Total	15	15	15	45	100

Source: Opinion Survey

From the above table has been clear that most of the respondent 62% through that tax administration is not effective to impose fines and penalties in Nepal. Only 38% respondent through that tax administration is effective to impose fines and penalties in Nepal. Most of the tax administrations are in favor with effectiveness of tax administration to impose fines and penalties because they don’t want show their weakness. Thus, it can be concluded that the tax administration of Nepal is not effective to impose fines and penalties.

In order to know the cause of ineffective tax administration the next question was asked. If no, what are the reasons? The respondents were requested to rank their answer, which are in the following table.

Table 4.25: Reasons of Ineffective Tax Administration to Impose Fines and Penalties

S.N.	Goals of income tax	Group			Total points	%	Rank
		A	E	P			
1.	Corruption	90	13	137	240	23	1
2.	Lack of information	75	15	94	184	17	3
3.	Lack of competent staff	83	17	107	207	19	2
4.	Complicated tax law	47	20	75	142	13	4
5.	Unnecessary outside pressure	35	15	67	117	11	5
6.	Lack of Co-operation in tax administration	45	14	40	99	9	6
7.	Lack of logistic support	25	19	35	79	8	7
Total					1068	100	

Source: Opinion Survey

The causes of ineffectiveness of Nepalese income tax administration to impose fines and penalties as per necessary were ranked in order of the preference of the respondent were as follows:

1. Corruption.
2. Lack of competent staff.
3. Lack of information.
4. Complicated tax law.
5. Unnecessary outside pressure.
6. Lack of Co-operation in tax administration.
7. Lack of logistic support

It can concluded that corruption, lack of competent staff, complicated tax law and lack of information is the most important causes of ineffectiveness of Nepalese tax administration to impose fines and penalties as per necessary.

4.7 Findings

On the basis of data presentation and analysis some important findings of this study are summarized below.

1. The study shows the contribution of tax revenue to Total Revenue was about in highest 81.14%, in lowest 75.74%, and that of non-tax revenue was about in highest 24.26% and in lowest 18.86% during the five years. It shows that tax has been a major source of revenue mobilization.
2. Tax revenue is the composition of direct and indirect tax in the Nepalese tax revenue. The contribution of tax revenue to total revenue was 75.74%, 77.29%, 77.16%, 79.45% and 81.14% from F.Y. 2002/03 to F.Y. 2006/07 respectively. It shows that the contribution of tax revenue is increasing trend. The contribution of indirect tax on total tax revenue from F.Y. 2002/03 to 2006/07 was 57.77%, 58.2%,58.53%,60.13% and 59.50%, where The contribution of direct tax on total tax revenue from F.Y. 2002/03 to 2006/07 was 17.97%, 19.09%, 18.63%, 19.32%, and 21.64% respectively. It shows the higher contribution of indirect tax than direct tax in total tax revenue.
3. Non-tax revenue is the composition of various components i.e. duties & fees, fines & forfeiture, public utilities, dividends, interest, royalty and sales of government property, principal repayments and miscellaneous income. The contribution of non-tax revenue on total tax revenue from F.Y. 2002/03 to 2006/07 was 24.26%, 22.71%, 22.84%, 20.55%, and 18.86% respectively. It shows that the contribution of tax revenue is decreasing trend. In comparison between tax revenue and non-tax revenue, the tax revenue is the main sources of government revenue.
4. Ration of direct tax in total revenue were 17.97%, 19.09%, 18.63%, 19.32% and 21.64% from F.Y. 2002/03 to F.Y. 2006/07 respectively. It shows increasing trend even though it was decreased in F.Y. 2004/05.

The direct tax in total tax revenue ratios were 23.73%, 24.71%, 24.14%, 24.31% and 26.67% respectively from F.Y. 2002/03 to F.Y. 2006/07. It shows constant trend till F.Y. 2005/06, than after it increased in F.Y. 2006/07. Even though ration of direct tax on total tax revenue is higher than ration of direct tax on total revenue, it is not increasing trend.

5. Income tax revenue is the composition of corporate income tax, remuneration income tax, investment income tax and other taxes in the Nepalese tax revenue. The growth rate of income tax were (9.49)%, 14.43%, 9.10%, 4.37% and 30.49% respectively from F.Y. 2002/03 to 2006/07. It shows that the growth rate of income tax is positively even though it was negative growth rate in F.Y. 2002/03.

6. The contribution of corporate tax to total income tax were 68.30%, 71.60%, 70.12%, 69.30% and 73.78% respectively from F.Y. 2002/03 to F.Y. 2006/07. The growth rate of corporate tax were (30.58)%, 18.38%, 7.18%, 3.24% and 34.71% respectively in the same year. It shows mostly total income tax depends upon in corporate tax. So corporate tax plays a vital role to contribute to national revenue.

7. Corporate tax is the part of income tax revenue. It is a direct tax and it's a main source of income tax revenue. The contribution of corporate tax to government revenue were 9.9%, 10.9%, 10.5%, 10.5% and 13.23% respectively from F.Y. 2002/03 to 2006/07. It shows in increasing trend.

8. The contribution of listed Merchant Bankers to total tax revenue and total government revenue was 0.04% and 0.03% in F.Y. 2002/03 and 0.07% and 0.05% in F.Y. 2006/07, which was the highest contribution percentage of total tax revenue and total revenue. The lowest contribution percentage of total tax revenue and total revenue was 0.02% and 0.03% in F.Y. 2003/04.

9. The contribution of listed Merchant Bankers to income tax and corporate tax was 0.19% and 0.28% in F.Y. 2002/03 and 0.30% and

0.41% in F.Y. 2006/07, which was the highest contribution percentage of income tax and corporate tax revenue and lowest contribution percentage of income tax and corporate tax was 0.16% and 0.22% in F.Y. 2003/04.

10. The contribution of listed Merchant Bankers to GDP was 0.004% in F.Y. 2002/03 and 0.007% in F.Y. 2006/07 which was the highest contribution percentage. The lowest contribution percentage was 0.003% in F.Y. 2003/04.

From the opinion survey of various respondents i.e. tax expert, tax administrators, taxpayers and bank officials, the following findings have been drawn.

- The main goal of income taxation in Nepal is increase the revenue of government.
- Income tax is a suitable source of mobilizing domestic resources. Main reason is harmful to depend fully on external sources.
- Lack of clear, transparent and progressive economic policy is the main reason for unsatisfactory with sound and effectiveness on income tax system o Nepal.
- Majority of the respondents are disagreeing with sound and effectiveness of income tax system of Nepal.
- Lack of clear, transparent and progressive economic policy is the main reason for unsatisfactory with sound and effectiveness on income tax system o Nepal.
- Existing corporate tax rate has been found suitable and single rate for all types of corporation is preferred.
- Delays in tax assessment are suitable in Nepal. Main reason is delays in filings returns.

- Main reason of complain of Merchant Bankers is about tax assessment system. Main reason for filing appeals by Merchant Bankers to revenue tribunal are order of tax assessment by tax authorities.
- Tax holiday is main reason of tax concession facilities and incentive to be given to the Merchant Bankers.
- Tax administration is not effective to impose fine and penalties as per necessary. Main cause of the ineffectiveness tax administration is corruption, lack of competent staff, complicated tax law and lack of honesty.

CHAPTER – V

SUMMARY, CONCLUSION AND RECOMMENDATION

In this chapter shows the final report of the study. This chapter divided in to three sections. First section deals with the summary, second section deals with the conclusion of the study and the third section of this chapter is remedies or recommendations of the study. The detail of this section is presented below:

5.1 Summary

Merchant Bank plays a vital role in economic and financial development of the country being work as a bridge, which provides every kind of financial assistances to industries and commerce. Merchant bankers are one of the pioneer instruments for business organization development. Basically objective of study of income tax collection from merchant bankers of Nepal is to evaluate contribution of income tax to government revenue and analysis the problem of merchant bankers in Nepalese context. They play a highly significant role in mobilizing funds of savers to ingestible channels assuring of promising return on investments and thus can help in meeting the widening demand for ingestible funds for economic activity. The service of merchant banker could cover project counseling and pre-investment activities, feasibility studies, project reports, design of capital stricture, issue management and underwriting, loan syndication, foreign currency finance, merger, amalgamations and takeover, venture capital and public deposits.

For the analysis of "A Study on Income Tax Collection from Merchant Bankers of Nepal" the data collection is an important thing where data collection specially primary and secondary methods are used. Annual reports of concerned institution, informal interview, questioner, frequent visiting the Security Exchange Board of Nepal, old thesis, and magazines are major sources of data collection.

The information are tabulated and presented in graph and table. Obtained data are analyzed through different elements and different heading like as corporate tax, tax revenue, non tax revenue, government revenue, gross domestic product and in other topics. Various types of statistical tool like mean, standard deviation, and coefficient of variation are also used in data analysis. Data presentation analysis chapter represents the presentation of whole data and analysis them. Basically the data is taken from fiscal year 2002/03 to 2006/07 AD.

For the Study of income tax collection from merchant bankers of Nepal especially I have chosen the seven institutions which are NMB Bank Ltd., Nepal Finance Company Ltd., Nepal Housing & Merchant Finance Ltd., Citizen Investment Trust, NIDC Capital Markets Ltd., Development Credit Bank Ltd. & Nepal Share Markets and Finance Ltd. During Fiscal Year 2002/03 to 2006/07 income tax collection from NMB Bank Ltd., Nepal Finance Company Ltd., Nepal Housing & Merchant Finance Ltd., Citizen Investment Trust, NIDC Capital Markets Ltd., Development Credit Bank Ltd. & Nepal Share Markets and Finance Ltd. were Rs.112.77 million, Rs.38.34 million, Rs.34.94 million, Rs.31.61 million, Rs.84.39 million, Rs.91.04 million and Rs.46.13 million respectively. In comparison within five years income tax collected from NMB Bank Ltd. was highest and Citizen Investment Trust was lowest. Corporate tax collection from above mentioned seven merchant bankers in F.Y.2002/03 was Rs.33.14 million which was 0.06% on total government revenue and 0.08% on total tax revenue, F.Y. 2003/04 was Rs.62.64 million which was 0.10% on total government revenue and 0.13% on total tax revenue, F.Y. 2004/05 was Rs.79.99 million which was 0.11% on total government revenue and 0.15% on total tax revenue, F.Y. 2005/06 was Rs 124.73 million which was 0.17% on total government revenue and 0.22% on total tax revenue, and F.Y.2006/07 was Rs.138.73 million which was 0.16% on total government revenue and 0.19% on total tax revenue.

In the context of income tax collection from merchant bankers I found that banks, development banks & finance companies are actively participated in merchant banking and most of public issue is also related with banks & financial institutions however most of the responses are related with weak regulatory provision. They focused on lack of specified governing power. There are various problems about income tax administration like, proper record about the number of income tax payers, defective selection of personnel, lack of training and education to tax payers and tax officers, undue delay in making assessment, lack of responsibilities of officials on their work, existence of corruption, and lack of motivation to concerned authorities etc. Because of the inefficiency of the administration and increasing corruption, people have to faith in the working of government and its organization.

The income tax is the vital source of the government revenue. In the contest of developing countries like Nepal government can not raise more income tax from corporation because high income tax may discourage the formulation of corporation. There is no proper supervision over the staff member of tax collection department corruption is the main problem of tax administration. There is no reliable and sufficient data for tax purpose. However Merchant Bankers assist government to collect its revenue though making profit from the financial transaction by rendering service to the public and business organization and pay income tax from their taxable income.

5.2 Conclusion

Lack of sufficient financial resources is the main constraints for economic development of Nepal. Nepal has been suffering from capital shortage to acquire the goal of economic growth. Nepal is not being able to collect necessary fund.

The expenditure of Nepalese government is increasing year by year. Therefore, it has been heavily relying on the external and internal debt to meet the budget deficit because of the low revenue collection compared to the total expenditure. Internal resources are preferable for suitable economic development. But Nepal has been found itself unable for proper mobilization for internal resources. Thus, fiscal deficit of Nepal has been increasing. To meet the expenditure, Nepalese government is trying to extract money or valuable contributing from its people through taxation. To solve the problem of fiscal deficit, income tax should play an important role and it has been considered as a good remedy to cure the growing resource gap problem in Nepal. But, it has not been mobilized efficiently and properly.

Currently income tax system of Nepal encompasses four taxes. They are: corporate income tax, individual tax, house and land tax and interest tax. Among them contributing of corporate sector is the highest. The Nepalese income tax system has introduced in the F.Y. 1959/60. The first elected government levied the first income tax and no specific act was made to define and to treat income tax. Since then four income tax acts has been implemented.

Securities Act 2063 permits its licensed institution to perform merchant banking activities subject to their paid up capital.. Merchant Bankers are all profit oriented organizations. They make profit from above mentioned financial transactions. Because of profit making corporate bodies they must pay corporate tax out of the profit they make after deduction of allowable expenses provided by income tax law.

Nepal has trade deficits from the very beginning of budgeting practice. Consequently, it has taking loans from various friendly countries and international organizations. But this is not permanent solution of the national budget deficit. For the permanent solution of this problem, the country is required to mobilize internal resource as far as possible.

Government revenue is the composition of various items of tax revenue and non-tax revenue. Each of them plays role in national operation and development but due to insufficiency of these revenues, it is being unable to operate socio-economic development programs as expected. There are interrelationship between resources mobilization and developed economy. Maximum revenue realization through internal sources is only possible when its economy is developed or boomed. Income tax is one of the sources that is potential and justifiable to increase. Education of taxation and morality in tax paying of taxpayer also help in maximizing realization of income tax. Corporate bodies also play important role in revenue collection to the government. Developing countries like Nepal also hope that corporate bodies are the taxpayers from whom considerable amount can be collected. Analytical studies regarding financial performance and tax paying trends of different corporate sector should be undertaken time to time recognize the probable increment of collectible tax from these sectors and tax problems that causes low tax collection so that correction of the problems could be done in time. This study had been undertaken considering these aspects.

5.3 Recommendations

On the basis of findings of the study, the following recommendations have been made for the sound and effective income tax imposition. Success of income tax system is highly depended upon the simplicity of income tax law. The following amendments have to be made in income tax law.

- The collection and tax assessment provision should be made clear and simple so those taxpayers would be encouraged to pay income tax.
- Income tax act, rules and regulation should be clear and simple for all the taxpayers as well as tax administration. It should more effective.
- The language should be simple and clear. In spite of using the vague meaningful words, clear-cut provision should be made.
- The effective implementation of provision of reward, prize and incentive should be granted to the taxpayers who pay tax voluntarily.
- The provision of fines, penalties and punishment should be implemented at effectively for income tax evaders.
- Timely revision should be made in the matter of income tax policy. The system of changing income tax policy with the change of government should better be avoided.
- There should be effectively implementation of provision of auditing.

Income tax administration in Nepal suffers from a number of interacting and interrelated problems, which have badly affected its productivity and image. Thus the following step should be taken by Nepal Government to improve tax administration.

- There should be established a monitoring unit of the implementation of income tax law, politics and programs.
- There should be separate corporate income tax act, rules and regulation.

- Co-ordination between tax policy, tax personal and other department must be established.
- Effective system of reward and punishment to the employee should be established.
- The administration should try to increase effective public participation to minimize the income tax evasion.
- All the tax personnel should be given comprehensive training on various aspects of taxation on regular basis. Such training to employees should be provided with the country as well as foreign countries. Besides these, seminars, meeting etc. should be held on regular basis.
- A single corporate tax rate should be imposed for all types of corporation.
- The tax assessment system should be scientific. The self-assessment tax system should be promoted and developed for the interest of taxpayers.
- The income tax needs to be strengthened both for revenue and socio-economic purpose. It is to be raised through broadening the base an effective enforcement and better tax compliance.
- Broadening its coverage must widen the tax base and institutions, which are philanthropic and non-profit oriented by name but profit earner and without service attitude.
- Formally 15% to 18% Tax GDP ratio is regarded as moderate standard but Nepalese tax GDP ratio does not maintain it the highest ration of it is not exceeding 10% during the study period. So the government should be increase the proportion/percentage of direct tax because its ratio is very low during the study period and the increment of this ratio or percentage is regarded as better than direct tax proportion.
- Contribution percentage of direct tax revenue on total tax revenue is very low. Corporate sector's income tax is a main source of direct tax revenue and Merchant Bankers income taxes are included in the corporate sector

income tax. So, government should increase the income tax from Merchant Bankers to increase the direct tax revenue.

- Income tax from Merchant Bankers as percentage of GDP is very fluctuating. It indicates the poor performance M.B.. So, M.B... should avoid such high fluctuation by improving performance.

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APPENDIX – I

QUESTIONNAIRE

Name: …………………………………. Designation: ………………

Office/Organization: ……………………………………………

Occupation: ……………………………

This questionnaire is concerned with a study on **"Income Tax Collection from Merchant Bankers of Nepal"** It would be very much appreciated if you could spare some of your valuable time for filling this questionnaire.

1. In your opinion, is income tax a suitable means of raising domestic resources in Nepal?

   a. Yes ( ) b. No ( )

2. If yes, why is it a suitable means for raising domestic resources? (Please rank)

   a. It is harmful to depend fully on external sources. ( )

   b. Among the internal source, taxation seems to be the most viable method. ( )

   c. It is not possible to cut the consumption level of people, as it is already too low. ( )

   d. Several limitations of public borrowings. ( )

   e. Others. ( )

3. Do you think that the income tax system of Nepal is sound and efficient?

   a. Yes ( ) b. No ( )

4. If no, what is the major problem of income tax system of Nepal? (Please rank)

   a. Incompetency in income tax policy rule and regulation. ( )

   b. Inadequate government economic policy. ( )

   c. Lack of appropriate assessment procedure. ( )

   d. Lack of honest, trained & competent tax personnel. ( )

   e. Others (Please specify) ( )

5. In your opinion, the existing corporate tax rate is satisfactory?

   a. Yes ( ) b. No ( )

6. If no, Please specify

   ………………………………………………………………………………

   ……………………………………………………………………………

7. What should be the goal of income tax in Nepal? (Rank your answer)

   a. Increase the revenue of government. ( )

   b. Reduce the gap between poor and rich. ( )

   c. Promote private sector for investment. ( )

   d. Reduce in unemployment. ( )

   e. Others (Please specify………. ( )

8. Do you accept that you make delay in tax assessment?

   a. Yes ( ) b. No ( )

9. If yes, what may be the reasons?

   i. Delay in filing returns. ( )

   ii. The assessment procedure itself takes long time. ( )

   iii. Inefficiency of tax authorities. ( )

   iv. Negligence of tax personnel. ( )

   v. Others (Please specify).

10. What type of complain do Merchant Banker make? Please, keep tic mark and write the reason in brief.

   i. About tax assessment. ( )

ii. About behaviors of tax personnel. ( )

iii. About fines and penalties. ( )

iv. About previous included in income tax law. ( )

v. About tax incentives. ( )

vi. Others (Please specify).

11. What may be the reasons for filing appeals by merchant banker to Revenue Tribunal?

i. Vague provisions of tax law. ( )

ii. Use of discretion by tax authorities. ( )

iii. Order of tax assessment by tax authorities ( )

iv. Tax evasion. ( )

v. Others (Please specify).

12. What type of tax concession facilities and incentive to be given to the merchant banker companies?

i. Tax holiday. ( )

ii. Investment credit ( )

iii. Carry forward of losses ( )

iv. Accelerated depreciation ( )

v. Tax rate deduction. ( )

vi. Other (Please specify). ( )

13. Do you think the tax administration of Nepal is effective to impose fines and penalties as per necessary?

a. Yes ( ) b. No ( )

14. If no, give reasons?

i. Corruption ( )

ii. Lack of information. ( )

iii. Lack of competent staff. ( )

iv. Complicated tax law. ( )

v. Unnecessary outside pressure. ( )

vi. Lack of cooperation in tax administration. ( )

vii. Lack of logistic support. ( )

viii. Others (if any …………………….) ( )

"Thank You for Your Kind Co-operation"

APPENDIX – II

1. Calculation of Mean, Standard Deviation and Coefficient of Variation of NMB Bank Ltd.

Year	Income Tax Paid (X)	$(X - \bar{X})$	$(X - \bar{X})^2$
2059/60	11.76	-10.79	116.43
2060/61	16.79	-5.76	33.23
2061/62	11.50	-11.05	122.20
2062/63	38.07	15.52	240.77
2063/64	34.65	12.09	146.23
Total	**112.77**		**658.86**

$$\bar{X} = \frac{\sum X}{n} = \frac{112.77}{5} = 22.55$$

$$\sigma = \sqrt{\frac{\sum (X - \bar{X})^2}{n}} = \sqrt{\frac{658.86}{5}} = 11.48$$

$$\text{C.V.} = \frac{\sigma}{\bar{X}} = \frac{11.48}{22.55} = 0.4$$

2. Calculation of Mean, Standard Deviation and Coefficient of Variation of Nepal Housing and Merchant Finance Ltd.

Year	Income Tax Paid (X)	$(X - \bar{X})$	$(X - \bar{X})^2$
2002/03	1.56	-5.43	29.48
2003/04	2.1	-4.89	23.9
2004/05	7.94	0.95	0.9
2005/06	10.04	3.06	9.34
2006/07	13.30	6.31	39.84
Total	**34.94**		**103.46**

$$\bar{X} = \frac{\sum X}{n} = \frac{34.94}{5} = 6.99$$

$$\sigma = \sqrt{\frac{\sum (X - \bar{X})^2}{n}} = \sqrt{\frac{103.46}{5}} = 4.55$$

$$\text{C.V.} = \frac{\sigma}{\bar{X}} = \frac{4.55}{6.99} = 0.65$$

3. Calculation of Mean, Standard Deviation and Coefficient of Variation of Development Credit Bank Ltd.

Year	Income Tax Paid (X)	$(X \text{ Z} \overline{X})$	$(X \text{ Z} \overline{X})^2$
2002/03	12.58	-5.63	31.68
2003/04	12.02	-6.19	38.33
2004/05	19.56	1.35	1.82
2005/06	21.10	2.89	8.37
2006/07	25.79	7.58	57.42
Total	**91.04**		**137.61**

$\overline{X} \text{ X} \frac{\phi X}{n}$ $\quad$ $\pm \text{ X} \sqrt{\frac{\phi(X \text{ Z} \overline{X})^2}{n}}$ $\quad$ $\text{C.V.} = \frac{\pm}{\overline{X}}$

$= \frac{91.04}{5}$ $\quad$ $= \sqrt{\frac{137.61}{5}}$ $\quad$ $= \frac{5.25}{18.21}$

$= 18.21$ $\quad$ $= 5.25$ $\quad$ $= 0.3$

4. Calculation of Mean, Standard Deviation and Coefficient of Variation of Citizens Investment Trust.

Year	Income Tax Paid (X)	$(X \text{ Z} \overline{X})$	$(X \text{ Z} \overline{X})^2$
2002/03	2.51	-3.81	14.54
2003/04	4.89	-1.43	2.05
2004/05	5.86	-0.47	0.22
2005/06	8.89	2.56	6.57
2006/07	9.47	3.15	9.91
Total	**31.61**		**33.29**

$\overline{X} \text{ X} \frac{\phi X}{n}$ $\quad$ $\pm \text{ X} \sqrt{\frac{\phi(X \text{ Z} \overline{X})^2}{n}}$ $\quad$ $\text{C.V.} = \frac{\pm}{\overline{X}}$

$= \frac{31.61}{5}$ $\quad$ $= \sqrt{\frac{33.29}{5}}$ $\quad$ $= \frac{2.58}{6.32}$

$= 6.32$ $\quad$ $= 2.58$ $\quad$ $= 0.41$

5. Calculation of Mean, Standard Deviation and Coefficient of Variation of Nepal Finance Ltd.

Year	Income Tax Paid (X)	$(X \text{ Z} \bar{X})$	$(X \text{ Z} \bar{X})^2$
2002/03	2.93	-4.74	22.45
2003/04	9.62	1.95	3.80
2004/05	6.06	-1.61	2.60
2005/06	7.03	-0.64	0.41
2006/07	12.71	5.04	25.39
Total	**38.34**		**54.65**

$\bar{X} \text{ X} \frac{\phi X}{n}$

$= \frac{38.34}{5}$

$= 7.67$

$\pm \text{ X} \sqrt{\frac{\phi (X \text{ Z} \bar{X})^2}{n}}$

$= \sqrt{\frac{54.65}{5}}$

$= 3.31$

C.V. $= \frac{\pm}{\bar{X}}$

$= \frac{3.31}{7.67}$

$= 0.43$

6. Calculation of Mean, Standard Deviation of and Coefficient of Variation NIDC capital Markets Ltd.

Year	Income Tax Paid (X)	$(X \text{ Z} \bar{X})$	$(X \text{ Z} \bar{X})^2$
2002/03	-	-16.88	284.87
2003/04	15.21	-1.66	2.77
2004/05	17.02	0.14	0.02
2005/06	26.19	9.31	86.73
2006/07	25.97	9.09	82.66
Total	**84.39**		**457.04**

$\bar{X} \text{ X} \frac{\phi X}{n}$

$= \frac{84.39}{5}$

$= 16.88$

$\pm \text{ X} \sqrt{\frac{\phi (X \text{ Z} \bar{X})^2}{n}}$

$= \sqrt{\frac{457.04}{5}}$

$= 9.56$

C.V. $= \frac{\pm}{\bar{X}}$

$= \frac{9.56}{16.88}$

$= 0.57$

7. Calculation of Mean, Standard Deviation and Coefficient of Variation of Nepal Share Markets and Finance Ltd.

Year	Income Tax Paid (X)	$(X - \bar{X})$	$(X - \bar{X})^2$
2002/03	1.8	-7.43	55.15
2003/04	2.01	-7.22	52.12
2004/05	12.07	2.84	8.09
2005/06	13.41	4.18	17.48
2006/07	16.85	7.62	58.08
Total	**46.13**		**190.92**

$\bar{X} = \frac{\sum X}{n}$

$= \frac{46.13}{5}$

$= 9.23$

$\sigma = \sqrt{\frac{\sum (X - \bar{X})^2}{n}}$

$= \sqrt{\frac{190.92}{5}}$

$= 6.18$

$\text{C.V.} = \frac{\sigma}{\bar{X}}$

$= \frac{6.18}{9.23}$

$= 0.67$