

# CONTRIBUTION OF INCOME TAX IN TOTAL REVENUE OF NEPAL



BY

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## **A Thesis Submitted to:**

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## RECOMMENDATION

This is to certify that the thesis

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***Entitled:***

**CONTRIBUTION OF INCOME TAX IN TOTAL REVENUE OF NEPAL**

*has been prepared as approved by this Department in the prescribed format of the Faculty of Management. This thesis is forwarded for examination.*

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**DECLARATUION**

I hereby declare that the work reported in this thesis entitled "Contribution of Income Tax in Total Revenue of Nepal," submitted to R.R.M. Campus, Faculty of Management, Tribhuvan University is my research work done in the form of partial fulfillment for the requirement of Master of Business Studies (MBS) under the supervision and guidance of Mr. Mohan Kumar Karn, Lecturer of R.R.M.Campus, Janakpur Dham Dhanusha.

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This thesis has been prepared as dissertation for the partial fulfillment of the requirements for the master degree course in management. It has been tried to cover empirical findings concerning tax in the context of Nepal. This study deals cover empirical findings concerning tax in the context of Nepal. This study deals system in Nepal and knowledge about the tax of different persons in Nepal. At this moment, I would not like to forget numerous suggestions, comments and instructions given by Mr. Mohan Kumar Karn, who is my supervisor and also a respected lecturer in R.R.M. Campus. This thesis is the outcome of his continuous encouragement, many helpful suggestions and comments.

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### **Acronyms**

B.S. : Bikram Sambat

Ed. : Education

MOF : Ministry of Finance

FNCCI : Federation of Nepalese Chamber of Commerce and Industry.

FY : Fiscal Year

GAAP : General Accepted Accounting Principle

GDP : Gross Domestic Product.

Govt. : Government

i.e. : That is

IMF : International Monetary Fund.

Mgmt : Management

MOF : Ministry of Finance

NCC : Nepalese Chamber of Commerce

No. : Number

PAN : Permanent Account number

Rs. : Rupees

RST : Retailer sales tax

SAARC : South Asian Association for regional co-operation

SN : Serial Number

TPIN : Tax Payers Identification Number

T.U. : Tribhuvan University

UN : United Nations

VAT : Value Added Tax

WST : Wholesaler sales tax

& : And



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# Chapter-1

## INTRODUCTION

### 1.1 General Background:

Nepal is a small landlocked developing country situated in South Asia. It lies between two large countries India and China. India and China are advanced than Nepal. The economic growths of the both countries are in increasing trend. Nepalese economy is affected by the both countries directly or indirectly. In this situation Nepalese economy cannot stay alone without considering these countries economy. On the other side, it is rich in natural resources. However, it is rich in natural resources; it is facing a number of problems. They are unemployment, poverty, rapid growth of population, political instability etc.

A country needs a lot of money to carry out development plans to fulfill its responsibility towards the citizens. So, it requires sufficient funds to carry out development activities, to handle day to day administration, maintain peace and security, lunch other public welfare activities and for creation of various socio economic infrastructures. If the government allocates the budget in this sector properly the Nepalese economy will increase near. But the government expenditure is increasing day by day because of various causes. To meet the expenditure, the government should collect fund from different sources. These sources may be tax and non tax. Non-tax sources include different revenues like gifts, grants, revenues from public enterprises, administrative revenues such as registration fees, fine and penalties. Almost 20% of revenues come from these sources.

Another source of government revenue is tax. It is the main source of revenue to the government. It includes customers, excise duty, vat, income tax, property tax etc. Nepal gets almost 80% revenue from these sources. 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. The definition of tax will be more clear from the following definitions.

*According to Findlays Shiras, "Tax is a compulsory contribution to public authorities to meet the general expenses of government which have been incurred for public good and without reference to special benefits."*

*According to Selingman, "Tax is a compulsory contribution from a person to the government to defray the expenses incurred in the common interest of all without reference to special benefits conferred."*

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

**From the above definition, it can be concluded that:**

- a) A tax is compulsory levy imposed by the government.
- b) It is collected from persons as per prevailing laws.
- c) Those who pay tax do not corresponding benefits from the government.
- d) The amount of tax is spent for common interest of all people.

Discussing about the historical development of income tax, the country Great Britain is the first country in the world to introduce income tax to generate revenue to finance war against France in 1799. USA introduced income tax in 1862 to generate revenue to finance civil war. India adopted income tax in 1860. The idea of introducing income tax in Nepal originated in early 1950s when a multi- party democratic political system was introduced. In 1951, the finance minister in his budget speech declared the intention of government to levy an income tax. The first elected government in 1959 finally introduced Business profits and balances Tax Act, 1960 in Nepal. After three years experience of income tax, the government replaced the prevailing Tax Act by Income tax Act, 1962. The act was amended for five times for Income tax Act 1974 (2031). This Act having 66 sections, classified into five groups (a) Agricultural (b) Industry, trade, Profession or occupation (c) Remuneration (d) House and compound Rents

(e) Other Sources.

The enhance revenue mobilization through effective revenue collection procedure for the economic development of a country and to amend and integrate the laws relating to income tax, the parliament of Nepal enacted Income tax Act 2002 (2058). Similarly the new income tax rules 2059 have also been enacted for the effective implementation of the objective of this Act.

The firm tax can be classified into two broad categories.

**Direct Tax:** The direct tax is a tax paid by a person on whom it is legally imposed. In direct tax the person paying and bearing tax is same. Income tax, property tax, vehicles tax, interest tax, expenditure tax, death tax, gifts tax and capital gain tax are examples of direct tax.

**Indirect Tax:** A tax imposed on one person but partly or wholly paid by other is called indirect tax VAT, sales tax, hotel tax; excise duty, import and export duty etc are examples of indirect tax.

To increase the government expenditure the government should increase his fund. To increase the government fund the government should increase the collection of tax. That is why, to get maximum benefits, the government should increase the collection of tax by adopting effective tax collection system.

## 1.2 Statement of Problem:

Nepal is an undeveloped country. There are many reasons behind its undevelopment. It is facing a number of problems. The government cannot operate the development project due to lack of sufficient amount of fund. Government expenditures are increasing day by day due to price level changes and other circumstances. It is in peace building process. The constitution is also under process. The government revenue is less than the government expenditure. Nepalese government is taking budgetary aid from foreign countries. Most of the industries are not properly in operation because of lack of fund. The government

has not succeeded to collect internal revenue properly. On the other hands, there are many negative results of foreign loans. The problems of Nepal are as follows:

- a) resources constraint
- b) massive poverty
- c) rapid growth of population
- d) unemployment problem
- e) political instability

To solve these problems, the government should create maximum employment opportunities. Business loan should be provided to those educated people who want to conduct business to generate income. Skill oriented training should be given to unemployed person. The government cannot perform these works properly in absence of sufficient fund. To generate sufficient amount of fund, it should collect tax.

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

The main objective of this study is to find out contribution of income tax in total revenue of Nepal. However the following specific objectives are set for the study.

- a) To find out revenue collection from the different year.
- b) To review the tax collection system.
- c) To find out contribution of income tax in total revenue.
- d) To find out the problems in tax collection system.
- e) To provide suggestion for effective tax collection.

### **1.4 Need and importance of Study:**

This study will be multidimensional importance for academic professionals, tax administrators, tax payers and general public who want to understand about income tax. This study is helpful to:

- a) The government of Nepal for raising fund internally.
- b) The economic development through the saving and investment procedure.
- c) Find out problem of tax and its remedies.
- d) Provide clear idea and knowledge to those persons who are interested to know about the tax system.
- e) Provide suggestions to different persons to make effective technique to collect income tax.

## 1.5 Research Methodology:

This study deals with the research design population and sample of data, data collection procedures and tools for analysis.

### **Research Design:**

To conduct the research analytical and descriptive research approach is adopted or the readily available historical data used in this study are primary and secondary data.

### **Population Sample:**

Tax payers, tax experts, tax administrators will consider as the total population out of them 25 tax experts, 25 tax administrations and 25 tax payers are considered as the target for the study.

### **Sources of data:**

The primary as well as secondary data are collected. The major sources of data are as follows:

- a) **Primary data**: Primary sources of data are collected in Janakpur municipality.
- b) **Secondary sources of data**: Secondary sources of data are collected from the information received from books, economic survey, published and unpublished articles, newspaper, annual reports etc.

### **Data Processing Procedure:**

To find out actual result different financial and statistical tools are used to analyze the information. Simply, these tools are used.

- a) Simple percentage
- b) Simple average
- c) Graphs, Charts and diagrams.
- d) Curvilinear model etc.

### **1.6 Limitation of the study:**

In the field of every study, there is some importance as well as limitation too. This study is not free from limitations. The main limitations of this study are as follows:

- a) The study is based on availability of reliable data and sufficient literature.
- b) Field survey is based on Janakpur city only.
- c) Field survey focuses only Janakpur city.
- d) This study includes around 7 year's data only.
- e) Limited businessman, tax experts, tax officers and customers are consulted to collect primary data.

### **1.7 Organization of the Study:**

This study is divided into five chapters. They are:

#### **Introduction**

The first chapter deals with background, statement problem, focus of the objective of study, research methodology, and limitation of study and chapter scheme.

#### **Literature review:**

The second chapter deals with the review related literatures and available studies, written and prepared by different experts and researchers.

**Research Methodology:**

The third chapter 'Research and Methodology' presents the methodology used in this study. It deals with research design, nature and sources of data, collection of data, data processing procedures and method of data analysis.

**Presentation and analysis of data:**

The fourth chapter fulfills the objectives of the study by presenting the data and analyzing them with the help of various accounting and statistical tools and techniques followed by methodology.

**Summary and Conclusion:**

The fifth chapter summarizes the whole study. Moreover it draws the summary conclusion and forwards the recommendation for the improvement of effective tax collection system and give up the problems in tax collection system.

## Chapter -2

### REVIEW OF LITERATURE

#### 2.1 Concept of tax:

Every government needs sufficient revenues to operate the development programme, to handle day to day administration, to keep peace and security and to conduct other public welfare programme. The Government collects revenues from various sources. Non tax revenues include revenues from Government Corporation and public enterprises, fees, special assessment, fines and penalties and foreign grants etc. Tax is the main source of collecting the public revenues because it occupies the most important part of government total revenue. In Nepal about 80% of total revenue comes from tax revenues and the 20% from non-tax revenues.

#### **Following are the main sources of government revenues:-**

- a) Tax: It is a compulsory contribution made by tax payers to the government without having any direct personal benefits.
- b) Price of goods and services provided by government. It is the amount collected from special sector for specific purpose.
- c) Receipt from public enterprises. The government's receipt amount from public enterprises owned by it.
- d) Fee: The amount paid for the government for receiving its services.
- e) Fines: It is the amount paid for breaking government's rules and regulations.
- f) Grants: The amount received by the government from other countries and international agencies.

Among all the above sources of the government revenues, tax is the major source covering most part of the government total revenue. It is a compulsory levy imposed by the government but it cannot be taken as fine. It is levied on persons as per prevailing laws. It is spent for common interest of people. It is collected from haves and spent for the interest of haves-not in the society. Tax

payers do not get any direct benefit from the state by paying tax. Government collects it with permission of legislature to fulfill financial need of the state. It is compulsory payment to government for the compensation of public welfare expenses. Tax fulfills the needs of central as well as local government. The main objective of tax is to distribute income and wealth equally among citizens. It can be mainly categorized into two groups. They are direct and indirect tax. It is a kind of revenue. So, it is a legal duty of every citizen to pay honestly. The experts have given definition regarding tax and some of them are explained here.

*According to Bastable, "A tax is compulsory contribution of wealth of a person or body of persons for the service of public power."*

*According to Dalton, "A tax is a compulsory contribution imposed by public authorities irrespective of the exact amount of service rendered to the tax payer in return and not imposed a penalty for any legal offence."*

*According to Prof, Seligman, "A compulsory contribution from a person to the government to defray the expenses incurred in the common interest of all without references to special benefit conferred."*

From the above definition, it is clear that a tax is a compulsory levy and those who are taxed has to pay it without getting corresponding benefit of services or goods from the government. Those who pay tax do not get corresponding benefits from the government. Tax collected is spent for common welfare of the people. It is collected from natural as well as artificial person. There are many tax systems in the world. However two types of tax system are in practice. They are: direct and indirect tax.

## **2.2 Objective of Tax:**

Tax is permanent source of collecting revenues. It is most important element of state system without it a state cannot be operated. It has been an instrument of social and economic policy for the government. In ancient times, the chief objectives of taxation were to make strong the muscles of nation by providing resources. At the times of Adam Smith; the main objective of collection



of tax was to provide resources to the government for providing security to an individual and society against violence, invasion and injustice and maintain public enterprises.

In modern times, the objective of tax is not only to maintain peace and security but also to conduct development activities. The objectives of tax are as follows:

- a. to raise more revenues
- b. to distribute income and wealth equally among citizens.
- c. to redistribute wealth for the common good.
- d. to increase the employment, saving and investment.
- e. to minimize regional disparity.
- f. to boost up the economy.

### **2.3 Classification of Tax:**

Taxes are classified into two groups. They are: Direct and Indirect taxes.

#### **A. Direct Tax**

The tax that is paid by the person to whom it is imposed is called direct tax. In this, the person paying and bearing tax is same. This tax is imposed to the income and property of citizens and organizations. Examples of direct tax are: Income tax, Vehicle tax, Expenditure tax, Property tax, Interest tax, Death tax, Gift tax, Casual gain tax etc.

#### **Merits:**

- a) It is equitable as it is imposed on a person as per the property or income.
- b) Time and procedure and amount of tax to be paid is known with certainty.
- c) It is elastic. The government can change tax rate with the change in income level.
- d) It enhances the consciousness of the citizens. Tax payers feel burden of tax and so they can insist the government to spend their contributions for the welfare of community.

**Demerits:**

- a) It gives mental pinch to the tax payers as they have to curtail the income to pay the government.
- b) Tax payers feel inconvenience as the government imposes tax progressively.
- c) Tax evasion may increase to avoid tax burden.
- d) It is an expensive tax collection system.

**B. Indirect Tax**

The tax which is imposed on one person but partly or wholly paid by another is called indirect tax. In this tax, the person paying and bearing the tax is different. It is the tax consumption or expenditures. VAT, Sales tax, Entertainment tax, Excise duty, Hotel tax, Import and export duty etc are the examples of indirect tax.

**Merits:**

- a) It is convenient as the tax payer does not have to pay a lump sum amount for tax.
- b) There is a mass participation. Each and every person getting goods or services has to pay tax.
- c) There is less chance of tax evasion as the tax payers pay the tax collected from customers.
- d) The government can check on the consumption of harmful goods by imposing higher taxes.

**Demerits:**

- a) It is uncertain. As demand fluctuates, tax will also fluctuate.
- b) It is regretful as the tax burden to the rich and poor is same.

- c) It has bad effect on consumption, production and employment. Higher taxes will reduce all of them.
- d) Most of the taxes are included in the price of goods or services. As a result, tax payers do not know how much tax they are paying to the government.

## **2.4 Canons of Taxation:**

The canons of taxation are the principles of taxation. They help to formulate suitable tax policy. They are widely accepted as providing a good basis by which to judge taxes. The 'Canons of taxation' were first developed by Adam Smith in his book entitled 'Wealth of Nation'. Some well known canons of taxation are as follows:

- a) Canon of Equity
- b) Canon of Certainty
- c) Canon of Economy
- d) Canon of Diversity
- e) Canon of Simplicity
- f) Canon of Neutrality
- g) Canon of Co-ordination
- h) Canon of Productivity
- i) Canon of Elasticity

## **2.5 Meaning of Income Tax:**

According to diverse economic structure nature of the government and status of people, the concepts of income tax is different in different country. In USA, Income tax is viewed as a matter of practice, recurrent is non-relevant to the tax status. In UK the original concept of the tax was that of a levy on recurrent income. Tax was applied to five schedules. Any item not falling within schedule was not subject to tax. In India, the

personal income tax is levied in the net income of all individual, Joint Hindu families, unregistered firm and other associations of person. (Chelliah, 1959)

Income tax is a personal tax. It is imposed on the net income of individuals and corporation. The income tax is defined in terms of the 'flow of wealth' of receipt in money or goods from tax payer during the period in USA and Canada. In flow of wealth method, tax is imposed on realization. Henu, tax is imposed on cash basis income. It applies only when a transaction occurs between other persons and tax payers.

According to the economists - An income tax is a levy imposed upon the income of individuals after the exemption limit. Income tax is a direct tax based on total income of the payer from all sources and is graduated on special system of exemption. Income tax is the most important single source of revenue of government of every country either it contributes more or less in total revenue.

It is very difficult to define income tax. Income, as the economic gain received by the person during particular period. Henry Simon has given the most satisfactory definition of income tax. According to him, Income tax is the sum total of the person's consumption and net increases in wealth during the period. Symbolically,

$$y = C + \Delta w,$$

Where,

$$y = \text{Income}$$

$$C = \text{Consumption}$$

$$\Delta w = \text{net increase in wealth}$$

It is very difficult to give clear and precise definition of income tax. So it is defined according to the income tax act of various countries. For example: According to income tax act 2058 (2002) sec. 2(h), income means a person income from any employment, business or investment and the total of that income as calculated in accordance with this act.

According to Indian Income tax act 1961 set 2. Income tax includes profits and gains, dividend, voluntary contribution received by Chain table trust, value of any

perquisite or profit on lieu of salary, and capital gain, winning from lotteries, cross word puzzles etc.

## **2.6 International History of Income Tax:**

Great Britain is the first country in the world to introduce a modern income tax. It introduced income tax in 1799 to finance the war against France. Only after 1980, it was accepted as a permanent tax. In United State, the first federal income tax was imposed in 1862 to generate to revenue to finance civil war expenditure. However it became permanent feature only in 1913 after 16<sup>th</sup> amendment to US. Constitution. In India, income tax was adopted in 1860. After introducing 'Income tax act 1886 in 1886, it was imposed as permanent tax. Italy adopted income tax in 1864, New Zealand in 1891, Australia on 1915 and Canada in 1917. After First World War, income tax became the most important source of tax revenue in developed countries it has become the most important source of revenue in most developed countries and had made appearance in a number of developing nations.

In the beginning of introducing time, it was generally levied at flat rate. After 1909, the Principle of progression was introduced from the UK and New Zealand. It was introduced due to the cause of war and national emergencies. So we can say income tax as war tax. After the end of war, the tax was named as income tax. It has become the most important for the equal distribution of wealth and prevention of poverty.

## **2.7 Historical Aspects of Income Tax In Nepal:**

### **A. Taxation in Ancient Nepal**

Income tax was the most important element of government revenue from ancient age. A few economic activities were operated in the country so government could not collect large amount of money in form of tax. In ancient time, taxes are imposed to the merchant, travelers and farmers in the form of cash, kind of labour. Sometimes gold and agricultural products were also paid as taxes. However, they were temporary in nature and they were raised for special purpose like war, sagas, religious works etc.

There is no relevant source of ancient tax. In the inscription of Anshuberma, it is noted that there were three taxes called 'Trikar'. Agriculture and animal husbandry tax was called 'Bhaga'. Business tax was called 'Kara'. Irrigation and religious monuments preservation tax was also in practice at the time of Anshuberma. Different types of taxes were imposed to generate maximum revenue during 1846-1968 AD. The major sources of revenue were, Birta and Kipat, taxes on land, monopolies, customs, transit and market duties, mines and mints and the export of forest products, birds, animals and various levies and fines. Taxes were collected at three levels. They were Royal palace levies, government levies and local levies. Various taxes imposed during that period were narrow in base and were imposed primarily on occupations and economic activities, not in income or property. There was not income tax in modern sense. Income tax from agriculture income and incomes from business were introduced as direct tax for the first time in our country Nepal.

## **B. Taxation in Nepal before Democracy**

The time from 1772 to 1950 has taken as before democracy period. During this period tax system became more advance than the ancient period. Taxation had a broad sense during this period. Revenue maximization was only the main objective of tax policies. Raikar, Birta, Guthi, Sera and Kipat were the five main land tax. Among them Birta and Kipat were the main source of revenue.

'Gadimubarak' was collected to finance coronation ceremony of a new king. 'Darshanbhet' was collected from both civil and military employees at the time of their appointment and confirmation. 'Salami' was collected as local revenue in terai region as annual payment. Taxes were levied on occupations and economic activity not in property. The base of tax was very narrow. The Birta owner class had much influential role in political & administration. In 1772 king Prithvi Narayan Shah introduced 'Pota tax' which was regarded as revolutionary measures in Nepal's fiscal system. 'Pota tax' was not based on progressive tax principle. It was limited on small Birta owners and privileged of the members of the nobility person did not pay 'Pota'. Only common people used to pay 'Pota tax'.

The major source of revenue were land tax, custom and excise duty in the form of lump sum contracts, royalties on forest, royalty on supply of porters and soldiers, entertainment tax and a few other minor taxes. Incomes were not taxed for raising regular revenues of state. It was collected to meet some specific expenditure like war and other emergencies.

In Nepal, there was no direct tax except land tax collected on a contractual basis and 'Salami' which the government employees used to pay out of their salaries at very small percentage. The 'Salami' was removed in 1951. At the time of Rana, effective revenue administration system did not developed. After the arrival of democracy in 1951, taxes are collected according to law in Nepal.

## **2.8 Income Tax in Modern Nepal:**

Income tax is a direct tax. It is imposed on the earning of individual and corporation. The tax which is imposed on taxable income of individual and corporation is called income tax. It is charged by government on the income of the previous year at the rate of prescribed each year by the finance act. This tax is based on canon of ability. It could be adjusted as to exempt the lowest income groups from the operation of the tax and make rich people bear the burden of tax according to their income. Tax economists suggest that income tax should be imposed upon income of individual after the exemption limit. All incomes above the exemption limit are subjected to income tax.

After 1951, the role of government has changed. Government's work is not only limited to maintain law and order and collection of revenue. It has enforced to operate development activities for the welfare of public. A sound and efficient income tax system is essential to maximize the revenue collection from income tax. Whole income tax system has made of three sub-systems. They are income tax policy, income tax laws and income tax administration. Income tax policy is made by the government itself through Ministry of Finance. It should be such that the main objective of the income tax can be achieved.

Parliament marks the laws to implement the various policies. No taxes shall be imposed and collected illegally. The government imposes and collects income tax

according to law. Interim constitution 2063 has made the clear provision about it. In 1960, a formal income tax act was enacted in accordance with the provision in Finance act 1959 for the first time in Nepal. After three years experience, the business profit and remuneration Act, 1960 was found. It was very narrow and vague. It was Income Tax Act 1962 was replaced by Income Tax Act 1974. Income Tax Act 1974 was also replaced by Income Tax Act 2002. Present legal provision of income tax is associated with Income Tax Act 2002, Income Tax Rules 2002 and Finance Act of concerned financial year.

#### **A. Business Profit and Salaries tax Act 1960.**

The government of Nepal introduced a formal income tax for the first time in Nepal in 1960 (2017 B.S.) in the form of 'Business Profits and Remuneration Tax'. Before the act, Finance Act was used to make the provision regarding income tax. According to this act Business profits and Remunerations income were subject to income tax but the revenue for these taxes should not be collected properly according to original estimates. It had 22 sections. The first was about short title, areas and commencement. Similarly second section was about definition and last section was authority to make regulations of government to regulate the tax act. According to this act, tax payment should be made within 35 days once the office and the tax payment to be made specified. Fine and penalty of Rs. 5000 to 500 used charge to them who do not pay tax and not submit account mentioned in the act. There was appeal system too; if any tax payer was not satisfied with regard to the order of tax assessment. Such tax payer could appeal within 35 days from the date of an order of tax assessment receipt.

#### **B. Income Tax Act 1962.**

This tax act came into force on July 1962 by replacing the Income Tax Act 1960. This tax act was introduced as per the articles 93 of the constitution. This act had 29 sections. As per section 6 of this Act annual statement of income should be submitted to the concerned tax officer by the persons having annual income than Rs. 6000. The statement should file within 35 days of completion of fiscal year. The salaries of diplomatic representative of foreign country, salaries of foreign non-Nepali citizen



working in the service of Nepal government, dividend paid to shareholders, income of Nagar panchayat, village panchayat, public organizations, educational institutions, Nepal Rastra Bank, allowances granted by NG to ministers, employees saving fund etc were considered as tax free income by Act. As per Act  $\frac{1}{4}$  income from agriculture was taxable and remaining  $\frac{3}{4}$  were considered as expenditure to earn such income. The act was experienced for 13 years and was considered inadequate with the changing situation of Nepalese economy. This act was amended at once in 1972. The main feature of this Act can be mentioned as follows. Income was defined as all kinds of income including income from business, salaries any professions, rent from house or land, investment in cash or kind, agriculture, insurance agencies and any other sources. The status of tax payers was defined on personal as well as residential for tax purposes. Carry forward of losses for a period of two year's provision was made on this act. The provision of reassessment of tax as well as rectification of arithmetic errors was also included in this act. In this Act, provision was made for the exemption of income tax for new industries for a period not exceeding ten years.

### **C. Income Tax Act 1974.**

Everything should be adjusted according to the changing environment. According to the change in the socio economic environment of Nepal. The income tax act 1974 was enacted. The act was divided in basic 66 sections. This Act was practiced for 28 years, almost three decades in Nepal. Through out this time the act was amended for eight times, ie in 1977, 1979, 1980, 1984, 1985, 1986, 1989 and 1993. The act had classified the incomes in five groups as: (a) Agriculture (b) Trade, Industry, Profession or occupation (c) Remuneration (d) House and compound and (e) Other sources. However the agriculture income was kept outside the tax net except few years, through the Finance Acts. This act had made provision for self assessment tax for the first time in Nepal. According to this act tax payers were required to keep accounts and records for their source of income and preserve the records for a period of six years. There were additional provisions of exemption from income tax. The former act had not provision regarding income from Gudhi, compensation for life insurance or after the expiry of the life insurance policy. It had clear certain definitions specially relating to the tax, tax

payer, taxable income, gross income net income, personal status of the tax payers and non-resident tax payers, assessment of tax, philanthropic work, nonresident etc beside this method of computing net income from each source including the deductions allowable had been specified.

#### **D. Income Tax Act 2002.**

To enhance revenue mobilization through effective revenue collection procedure for the economic development of nation, and to amend and integrate the laws relating to income tax, the parliament of Nepal enacted Income Tax Act, 2002 (2058). This Act has replaced Income Tax Act 1974 (2031). This Act is quite advance Income tax that has ever introduced in Nepal. The main feature of this act is all the related matters within one Act. The Act is independent to levy income tax. This Act has 24 chapters and 143 sections. Amended Income Tax Act 2002 has dismissed the section 66. This Act has defined three different sources of incomes: (a) Business (b) Employment (c) Investment. Tax rates are different for different income groups. They vary as per individual and entities. There are clear provisions about depreciation rates, methods for all the five categories of depreciable assets. There are also provisions regarding international taxation, capital gain taxation, Penal provisions, appeal system. All matters income tax can be found within this act.

#### **Following are the main features of Income Tax Act 2002.**

- a) Income tax related all provisions are included within one act.
- b) This Act has clearly specified the amounts should be included while calculating a person's taxable income from conducting business or investment for an income year.
- c) All the expenses are allowed to deduct provided that the expenses are made by the same tax payer in the same year in the production of income.

- d) There is the provision of carry forward of loss for business or investment. Business and investment loss can be carried forward up to next 7 years while banking and general insurance business can carry backward the loss to preceding five income years.
- e) Incentives are provided to infrastructure constructor, hydropower projects and special industries.
- f) Now the economy of the most of the countries in the world is open one. The provision has introduced in the tax law related to international taxation. Transfer pricing, foreign tax credit, double taxation avoidance agreement etc are the provision of international taxation.
- g) This act has given the option for husband and wife as a separate natural individual until they do not accept as a couple.
- h) Capital gain, dividend etc has brought in tax net.
- i) Authorities of taxpayers have specified.
- j) To control tax evasion, provision of transfer pricing, thin capitalization, dividend stripping has made.
- k) Provision of fines and penalties have made more stringent in the new Income Tax Act 2002.
- l) This act has made a provision of relaxing the submission of income statement by a person who does not have taxable income and one who has the income from remuneration only.
- m) There has the special provision for deduction pollution control and research & development expenses.
- n) The income of an approved retirement fund is free from tax. But retirement payments in hand of employees are taxable.

- o) Resident persons are taxed in their worldwide income while non-resident persons are taxed only in their income sources in Nepal.
- p) The pool system of depreciation of fixed assets has introduced at first time. All types of assets are classified into five categories. Depreciation rate for classes A, B, C, D is based on diminishing balance method but straight line method for class 'E' (Intellectual Assets)
- q) There is facility of medical tax credit in this act. A resident individuals may claim medical tax credit of 15% of the amount of approved medical expenses and unabsorbed medical expenses can carry forward forever.

## **2.9 Head of Income:**

This Act has made the classification on incomes in three main categories. The sources of income have classified for the purpose of assessment under the following heads:

### **A. Income from Employment**

According to Income Tax Act 2002 section 2 (a) "employment includes a past, present or prospective employment." The act of performing a certain job for the person, who appoints one for the job, in consideration of a regular payment is called as employment. In other words, the payment or benefit received either in cash or kind with the help of labor is defined as employment income. It is the remuneration from the employment of an individual. There are two parties in the employment. They are employer and employee. Whatever the employee receives from employment in the shape of regular salary, allowances, overtime payment, bonus etc is included in the income from employment.

In common sense, an employment is meant as a long term employment. But in the eyes of law it may be short term also. It may be part time or full time. A single person may have more than one employment on a day.

The person who provides employment may be any natural as well as an artificial person. They may be like an individual (a sole trading concern), an entity, N.G., a local body or NG, an institution, an organization, a foreigner etc but the employee is always an individual (a natural person). A couple working in the same entity are treated as creation of two employments, one for husband and another for wife. The employee must be present physically at the place of work to perform his or her duties. The employee is awarded on the basis of his or her ability, education, experience, honesty, behavior etc and so a proxy is now here allowed to do work on behalf of the employee.

A written appointment letter does not always qualify an individual to be an employee but an oral employment or even the behavior of the employer and employee is sufficient to treat the individual as an employee. All the amounts or benefits received in connection with employment are taxable. As per section 8(2) the remuneration or income from employment for a income year include the following payments made by the employer:

- a) Payments of wages, salaries, gifts, bonuses and other facilities;
- b) Payments of any personal allowance, including any cost of living subsistence, rent, entertainment and transportation allowance;
- c) Payments providing any discharge or reimbursement of costs incurred by the individual or an associate of the individual;
- d) Payments for the individual's agreement to any conditions of the employment;
- e) Payments for redundancy or loss or termination of the employment;
- f) Retirement contributions (i.e. provident fund gratuity etc) including those paid by the employer to a retirement fund in respect of the employee, and retirement payments;
- g) Other payments made in respect of the employments; and
- h) Other quantified perquisites;

- i) Availability of motor vehicle wholly or partly for private purpose.
  - 1) 0.5% of salary in case of employees.
  - 2) 1% of market value of vehicle in case of other (i.e. consultant)
- j) The amount of difference of interest on loan paid by employer lower rate than market rate.
- k) Market value of assets in case of transfer of assets.
- l) For the payment other than stated above, the value of benefit of the payment to a third person.

## **B. Income from Business**

A business may be an industry a trade, a profession, or the like isolated transaction with a business character and includes a past, present or prospective business according to income tax Act 2002. It is an earning activity typically consisting of not only the provision of labor but of the combined provision of labor and capital. A person's income from a business for an income year is the person's profits and gains from conducting the business for the year. Business income is also a source of income in the eyes of income tax act 2002. Section 7 of income Tax Act, 2002 deals with the receipts or receivables to be included in income from business and section 13 and 19 deals the allowance expenses there from. Business includes trade, commerce, production, profession, vocation etc.

### **Trade and commerce**

The Oxford Dictionary defines trade as follows:

- a) The exchange of goods and services for money or other goods.
- b) Buying and selling.
- c) To buy and sell a particular item, product, etc.

The activity of a trade starts from the moment a good purchased or otherwise acquired with an intention to sell it for some profit. It is not necessary that the goods are sold in due course and profit is acquired there from.

It is not only the purchase and sale of goods that constitutes a trade but a sale of service is also included in the definition. The transportation of good and human beings, tourism etc are examples of the trade services. Though commerce is some things similar to trade, it is used especially when the trade takes place between two countries.

### **Production**

The dictionary meaning of production is "to make or manufacture something especially in large quantities". The process of production may be manual or based on machinery. The machinery may or may not run by power. A production is a process whereby the form of a good is changed and the new product acquires a new commercial value.

### **Profession and Vocation**

A profession is a paid occupation, which requires advanced education or training. Chartered accountants, lawyers, Architects etc are some examples of profession. A vocation is also paid occupation and requires practice and skill but it does not require advanced education. Carpenters, craftsmen, etc are the examples of vocation.

For the purpose of computing income of business for any year of income, the income of such person shall include as profits or gains by him from business and should include

- a) Service charge (Sec. 7.2)
- b) Sales or disposal of business / trading stock (Sec 7.2)

- c) Net gain from the disposed of person's business assets / liabilities of the business calculated under sec. 7.2
- d) Amount receives against the disposal of depreciable assets. (Sec. 7.2)
- e) Prize or gift in connection with business. (Sec.7.2)
- f) Amount received instead of acceptance of any restriction regarding business (Sec.7.2)
- g) Amount included under change of accounting method. (Sec.24)
- h) Excess amount received due to exchange rate of currency. (Sec. 28)
- i) Bad debt recovered. (Sec.25)
- j) Proportionate amount under long term contract. (Sec.26)
- k) Under paid interest amount according to market price. (Sec.)
- l) Amount received for compensation. (Sec.31)
- m) Other amount received under business income. (Sec.7.2)

(Income Tax Act, 2002)

While computing income tax from business, the following amounts are excluded on profit and income from business for tax purpose.

- a) Exempt amounts under section 10.
- b) Taxation of dividends under section 54.
- c) Final withholding payment under section 92.

(Income Tax Act, 2002)

**C. Income from Investment:-**

Section 2(a.1) defines investment as the holding of one or more properties or the investment in a property subject to the fact that:



- a) The property should not be used by the owner himself; or
- b) The property must not be a business or an employment.

The section further says that the holding of a non-business chargeable asset is also known as an investment. Investment in general sense is an act of letting out a property by an owner to somebody else for its exclusive use for the period of letting out. An amount given to another person for his utilization is also said to be an investment. The three points are the basic requirements for an investment are:

- a) A person has the legal ownership of a property;
- b) The owner transfers the right to use the property to another person; and
- c) For such a transfer of right the owner receives certain consideration from the transferee.

Section 9 (Income Tax Act, 2002) deals with the receipts or the receivables to be included in income from investment. Section 13, 14, 15, 16 and 19 deals with the deductions to be made while computing the taxable income. (Income Tax Act, 2002).

- a) Any dividend, interest, natural resources payment, rent, royalty, gain from investment insurance, gain from an unapproved retirement payment or retirement fund from approved retirement fund. (Sec.9.2)
- b) Net gains from the disposal of the person's non business chargeable assets of investment. (Sec.9.2)
- c) Excess amount of incomings over the depreciation basis including outgoings on the disposal of the depreciable assets of the investment of the persons. (Sec.9.2)
- d) Gifts or prizes received in connection with investment. (Sec.9.2)
- e) Retirement, contribution including those paid to retirement funds in respect of the person and retirement payments on respect of investment. (Sec.9.2)
- f) Amount received instead of acceptance of any restriction regarding investment. (Sec.9.2)

- g) Amount included under change of accounting method. (Sec.24)
- h) Excess amount received due to exchange rate currency. (Sec. 28)
- i) Bad debt recovered. (Sec. 25)
- j) Proportionate amount under long term contract. (Sec. 26)
- k) Under paid interest amount according to market price. (Sec.)
- l) Amount received as compensation. (Sec.31)
- m) Other amounts required to be included on tax accounting or qualification, allocation and characterizations of amounts or transaction between any entity and beneficiary or general insurance business. (Sec. 9.2)

(Income Tax Act, 2002)

## **2.10 Taxpayer / Person**

The Income Tax Act classifies tax payers into two types: an individual and an entity (Sec.2). The word "Person" is used for each taxpayers irrespective of its status. Thus the term "Person" includes:

- a) An Individual; or
- b) An entity

### **(a) Individual**

The term "Individual" is defined by sec.2 (ac) as follows;

- 1) A natural person;
- 2) A Proprietorship firm 100% owned by a single natural person; and
- 3) A couple elected as single natural person under Sec. 50.

The act has no provision for an undivided family to be regarded as a single tax payer. Each of the spouses is treated as separate natural person for tax assessment. However, Section 50 of the act has made provision that a couple can choose to be treated as single individual for a particular Income Year. In case the couple elects to be a single individual, the incomes of both the spouses shall be taxed in a single hand as that of one individual. However the following options have been made for individual.

- 1) The option is applicable even if either of the spouses is a non-earning member.
- 2) The couple is permitted to be treated as single individual taxpayer irrespective of whether such an option was taken in any previous year.
- 3) In case the couple has chosen to be treated as a single individual for tax purpose, either of the spouses will be either jointly or separately responsible for the payment of the tax.
- 4) The option is allowed only to a married couple, if each of the spouses is alive on the date of signing the tax return for the Income year. Because the next couple has to sign on the Tax Return as a token of the acceptance of the election.
- 5) Either of the spouses can be an assessee and the next spouse may give the consent. (Agrawal, 2004)

### **Provision for Individual Taxpayer under Income Tax Act, 2002**

#### **a. Allowable deduction**

##### **1. Retirement contribution to an approved retirement fund:**

The amount contributed to an approved retirement fund [Provident Fund (PF)], Citizen Investment Trust [CIT] and other approved retirement fund is allowed for deduction up to a specified limit.

i.e. - Actual Contribution (employees + employee)

Or 1/3 of assessable income

Or Rs. 300000

Whichever is less

The retirement contribution made to an unapproved retirement fund is not allowed for deduction.

## **2. Donation to tax exempt organization :**

Donation paid to tax-exempt organization registered at IRD may be deducted from taxable income under the following conditions-

i.e. - Actual donation

or 5% of Adjustable taxable income

or Rs. 100000

whichever is less

However, the government of Nepal may prescribe, by a notification in the Nepal Gazette, as to allow full or partial deduction at the time of assessing income of the expenses incurred for special purpose or donation given by the person.

Expenditure incurred by a company for the protection and promotion of ancient, religious and cultural heritage located in Nepal and for building public physical infrastructures of sports are allowed for reduction up to Rs. Lakhs or 10% of assessable income whichever is lower. However preapproval of IRD is required to take this facility.

## **3. Exemption Limit:**

Exemption limit is available only for the resident natural person. There are four types of exemption limit available only for the resident person.

- a) Basic exemption: Basic exemption is available only for resident natural person as per his family status.

Single / Unmarried / Individual	115000
Couple / Married	140000

- b) Additional exemption limit is available for the resident natural person (both for single and couple) working (residing) in remote areas of Nepal.

Remote areas	Additional Exemption Limit
'A'	Rs. 30,000
'B'	Rs. 24,000
'C'	Rs. 18,000
'D'	Rs. 12,000
'E'	Rs. 6,000

- c) For Pension income: A resident natural person (both for single and couple) having pension gets 25% additional exemption limit. But should not be more than pension income.

Single / Individual	$115000 \times 25\% = \text{Rs.}28750$
Couple / Married	$140,000 \times 25\% = \text{Rs.}35000$

- d) Life Insurance Premium (LIP): Life Insurance Premium paid by a resident natural person for his own life is allowable for deduction from taxable income up to the following limit:

Actual Premium paid

Or, 7% Insured Sum

Max Rs. 20,000

Or, Actual

Whichever is less.

#### **4. Medical Tax Credit**

Approval medical expenses incurred for a resident natural person can be claimed for a resident natural person can be claimed for deduction from his/her tax liability up to a specified limit:

Allowable medical tax credit:

15% of eligible medical expenses

+ Any amount carried forward from the previous year

Or, Rs. 750

Whichever is less

Note: For non-resident natural person no tax exemption limit of any kind is available and charge 25% flat tax rate. And special additional fee is charged on total taxable income of non-resident natural person. But 5% rebate on remaining slab is get if the income is derived by operating special industry or from export business.

### **2.11 Tax Exempt Incomes under this Income Tax Act**

- a) Amount derived by person entitled to privileges under a bilateral or a multilateral treaty conducted between Nepal Government and a foreign country or an International organization (like - employment income of foreign diplomats and employment income of UN representative)

- b) Remuneration under the employment of public services of a foreign government.
- c) Remuneration paid by NG to foreign citizen on terms of tax exemption.
- d) Pension received by retired army / police from public fund of foreign government.
- e) Allowance paid by NG to widow, elder citizen, disabled person.
- f) Amount derived by ways of gift, bequest, inheritance or scholarship except as required to be include in calculating income under business, investment, or employment.
- g) Agricultural income otherwise then a firm, company, partnership and registered corporate body and by those who has not holding of land more then as prescribed in land act, is non-taxable income.
- h) Income and dividend distributed by co-operative societies registered under co-operatives act, 2048 is non-taxable income.

## 2.12 Specimen for computing Income

### (A) Computation of Income from Business

#### As per Income Tax Act, 2058

Particulars	Amount
<b>Amount to be included</b>	
Service Charge (Sec.7.2)	xxx
Disposal of trading stock (Sec. 7.2)	xxx
Net gain from disposal of business assets or liability (Sec. 7.2)	xxx
Gain from disposal of pool of depreciable assets (Sec. 7.2)	xxx
Prizes or gifts in connection with business (Sec. 7.2)	xxx
Amount received in lieu of accepting any restriction regarding business (Sec. 7.2)	xxx
Amount received from any investment directly related to	xxx

business (Sec.7.2)	
Incomes to be included due to change in accounting methods (Sec.22.6)	xxx
Excess amount received due to exchange rate variation (Sec. 24.4)	xxx
Bad debts recovered (Sec. 25.1)	xxx
Proportionate amounts received under long term contracts (Sec. 26.1)	xxx
Under payment of interest according to market rate (Sec. 27.1)	xxx
Receivables amounts paid to others (Sec. 29)	xxx
Amount received for compensation (Sec. 31)	xxx
Other amounts received under the head of business income	xxx
<b>Gross income from business (A)</b>	xxx
<b>Allowable Deduction</b>	
Interest Expenses (Sec. 14)	xxx
Cost of trading stock (Sec. 15)	xxx
Repair and improvement cost (Sec. 16)	xxx
Pollution control cost (Sec. 17)	xxx
Research and Development Cost (Sec. 18)	xxx
Depreciation allowance (Sec. 19)	xxx
Reserve fund for banks (Sec. 59)	xxx
Other expenses	xxx
<b>Total Allowable deductions (B)</b>	xxx
<b>Assessable income from business before loss adjustment (A-B)</b>	xxx
Less: Adjustment of business losses (Sec. 20)	xxx
a. Unrelieved loss from other business this year (Sec 20)	xxx
b. Unrelieved loss from business of previous years (Sec 20)	xxx
<b>Total adjustable business loss [(a+b) = C]</b>	xxx
<b>Assessable income from business (A-B-C)</b>	xxx



**B.**

**Computation of Income from Investment**

**As per Income Tax Act, 2058**

<b>Particulars</b>	<b>Amounts</b>
<b>Amount to be included</b>	
Dividend payment (except final withholding payment (Sec. 9.2)	xxx
Gain from Investment Insurance (except final withholding payment Sec. 9.2)	xxx
Interest received (except final withholding payment (Sec. 9.2)	xxx
Rent received (except final withholding payment (Sec. 9.2)	xxx
Payment received from natural resources (Sec. 9.2)	xxx
Royalty Income (Sec. 9.2)	xxx
Gain from unapproved retirement fund (except final withholding payment (Sec. 9.2)	xxx
Gain from disposal of pool of depreciable assets (Sec. 9.2)	xxx
Gain received by the person in respect of the investment (Sec. 9.2)	xxx
Retirement contributions, including those paid to a retirement fund in respect of the person (Sec. 9.2)	xxx
Amounts received in lieu of accepting any restrictions regarding investment (Sec. 9.2)	xxx
Incomes to be included due to change in accounting methods (Sec. 22.6)	xxx
Excess amounts received due to exchange rate variation (Sec. 24.4)	xxx
Bad debts recovered (Sec. 25.1)	xxx
Under payment of interest according to market rate (Sec. 27.1)	xxx
Receivable amounts paid to others (Sec. 29)	xxx
Amounts received for compensation (Sec 31)	xxx
Income received from Joint investment (Sec 30)	xxx
Other amounts to be included under investment income	xxx

<b>Gross income from investment (A)</b>	xxx
<b>Allowable Deductions</b>	
Interest Expenses (Sec. 14)	xxx
Depreciation allowance (Sec. 19)	xxx
Others expenses related to investment	xxx
<b>Total Allowable deductions (B)</b>	xxx
<b>Assessable income from investment before loss adjustment (A-B)</b>	xxx
<b>Less: Adjustment of losses</b>	
a. Unrelieved loss from business or other investment this year (sec 20)	xxx
b. Unrelieved loss from business previous year (Sec 20)	xxx
<b>Total adjustable loss (C)</b>	xxx
<b>Assessable income from investment (A-B-C)</b>	xxx

C.

## Computation of Income from Employment

As per Income Tax Act, 2058

Particulars	Amounts
<b>Amount to be included</b>	
Salary and wages (Sec 8.2)	xxx
Leave pay (Sec 8.2)	xxx
Pay for overtime (Sec 8.2)	xxx
Fees (Sec 8.2)	xxx
Prizes and gifts relates to employment (Sec 8.2)	xxx
Bonus (Sec 8.2)	xxx
Other facilities (Sec 8.2)	xxx
Commissions (Sec 8.2)	xxx
Dearness Allowance (Sec 8.2)	xxx
Cost of living (Sec 8.2)	xxx
Rent (Sec 8.2)	xxx
Entertainment and transportation allowance (Sec 8.2)	xxx
Other Personal allowances (Sec 8.2)	xxx
Reimbursement of personal expenses (Sec 8.2)	xxx
Payments for the individual's agreement to any condition regarding employment (Sec 8.2)	xxx
Redundancy or loss related payments (Sec 8.2)	xxx
Other payments made in respect of employment payment (Sec 8.2)	xxx
Retirement payment & contribution to retirement fund (Sec 8.2)	xxx
Amounts of Vehicles facility (Sec 27.1)	xxx
Amounts of services of house keeper, chauffeur, gardener, or other domestic assistants (Sec. 27.1)	xxx
Any meal, refreshment or entertainment provided by employer (Sec 27.1)	xxx
Amount of services related to drinking water, electricity,	

telephones, and the like utilities in respect of the payees (Sec. 27.1)	xxx
Under paid interest by employee to employer for loan taken by the employee (Sec. 27.1)	xxx
Other amounts to be included	xxx
<b>Gross Income from employment</b>	xxx

**D. Statement of Total taxable income**

<b>Particulars</b>	<b>Amounts</b>
Assessable income from Employment	xxx
Assessable income from Business	xxx
Assessable income from investment	xxx
<b>Total assessable income</b>	xxx
Less: Allowable reductions	xxx
a. Donation (as per tax law) (Sec. 12)	xxx
b. Retirement contribution (as per tax law) (Sec 63)	xxx
<b>Total taxable income</b>	xxx

**E. Statement of Income tax liability**

<b>Particulars</b>	<b>Amounts</b>
First Rs. 115000 (individual), 140000 (Couple)	xxx
Next Rs. 85000 @ 15%	xxx
Balance Rs. xxx @ 25%	xxx
<b>Total tax liability</b>	xxx
Less: Advance tax paid	xxx
Medical tax credit	xxx
<b>Net tax to be paid</b>	xxx

### **2.13 Methods of Income Tax Assessment**

Income Tax Act, 2058 has specified three types of assessment. They are as follows:

- a) Self assessment (Sec. 99)
- b) Jeopardy assessment (Sec. 100)
- c) Amended assessment (Sec. 101)

Self assessment is done by the assesses himself whereas jeopardy and amended assessments are the assessments based on judgment of the Department.

### **2.14 Installment payment**

There is a provision of payment of income tax of the current year by three installments that is 40%, 30% and 30% by the end of Poush, Chaitra and Ashad respectively.

### **2.15 Appeal**

The taxpayer who is not satisfied with the assessment made by tax officials can lodge an objection against the assessment with the Director General (DG) of Inland Revenue Department or go to Revenue Tribunal. The Act has made it mandatory for the taxpayers first to file an objection with the Inland Revenue Department for an administrative review and then if unsatisfied with the decision of Director General, he/she can go to Revenue Tribunal.

## **2.16 Offences**

Offences are dealt within the Act in a sense of criminal offences of taxpayers as well as tax administrators. They lead to punishable in the form of fines and imprisonment on conviction. The offences attracting both a fine and the imprisonment include failure to comply with the Act, failures to pay tax, maintaining documentation or filing income returns and statements of estimated tax, making false or misleading statements, impeding or coercing the tax administration, offences by the authorized and unauthorized persons, offences of aiding or abetting, etc. In case if the Tax Return file is not submitted within the period prescribed by the Act, the late fee and interest amount will be charged at the rate of 0.1% per year of the assessable income.

## **2.17 The Super Act**

This tax act is super in regard to all income tax matters. No other Acts except this Act had made capable to make changes, amendment and other tax related provisions other than the provisions relating to imposition, assessment, reduction, increment, exemption or remission of tax to be made by amending this act itself by annual Finance Acts.

## **2.18 Review of Literature**

Income tax was imposed in Nepal by the first Parliamentary Government in 1959. Thereafter, various studies were made and researches conducted by different individuals and institutions concerning with various aspects of this act such as the structure, role, productivity, legal and administrative framework etc. Some of the books reports and dissertations that are reviewed during this study are as follows.

## 2.19 Review of Books and Reports

In 1965, Mr. Kedar Bahadur Amatya, published a book "Nepal Ma Aayakar ko Bebastha" in 1965. He has tried to describe about income tax and provision regarding income tax. His contribution was first in the field of income tax in Nepal. Basically, he analyzed legal aspect of income tax in Nepal at that period. (Amatya 1965)

Lent (1968), has presented a report entitled, "Survey of Nepalese tax structure" under the request of IMF, Fiscal Affairs Department. He has critically analyzed the scope of income tax in Nepal, tax structure, taxable income exemption and allowances given at that time. He has suggested reforming both the income law and administration to increase government revenue through income tax (Lent, 1968).

The book published in 1967 by Nirmal Bhattarai and Ratna Shrestha, gave information about the legal aspects of taxation in Nepal of that period.

In 1978, Dr, Govinda Ram Agrawal leaded a research team. A senior research officer of CEDA has conducted a research in the topic 'Resource Mobilization for development. and reform of income tax in Nepal.' This research report was published by CEDA, Kathmandu. Agrawal and this team have focused their study to analyze the various aspects of income tax in Nepal. The period covered by this study was twenty - Eight from 1951/52 to 1978/79. Both primary and secondary sources of data were used to conduct this study. Some of the important objectives of this study were as follows:

- a) To examine the problem of growing resource gaps in Nepalese finance in the context of the role of income tax.
- b) To examine the buoyancy and elasticity of income tax in Nepal including projection of income tax.
- c) To examine new personal for mobilization of additional domestic resources from income tax in Nepal.
- d) To examine possibilities for making income tax as policy instrument for reducing inequalities of income and wealth in Nepal.

- e) To examine the ways and means for increasing tax consciousness in the Nepalese public.

Mr. Agrawal and his team, in this study, have pointed out various findings and recommendations. Some significant findings and recommendations of this research were as follows:

- a) Needs for additional resource mobilization was growing by 85 times in Nepal and she was experiencing a serious and growing problem of resource gap.
- b) Income tax administration in Nepal suffered from a number of interacting and inter-related problems, which have badly affected its productivity.
- c) Income tax has been a fast growing category of tax revenue in Nepal.
- d) More than 50 percent of the total income tax revenue was contributed by the individuals' taxpayers.
- e) Buoyancy of income tax with respect to GDP for period 1967/68 to 1975/76 was 2.18 and elasticity was 2.01 since both buoyancy and elasticity were greater than unity; income tax in Nepal was positively responsive to change in GDP.
- f) The main defects of the income tax administration was failure to locate new tax payers, to maintain the proper accounts, delay in assessment, poor taxpayers compliance, evasion and avoidance of tax. And defectives management.

### **Recommendations**

- a) Additional domestic resources should be mobilized through taxation.
- b) Tax structure of Nepal need to is redesigned in order to increase the role of direct tax.
- c) Income tax should be reformed in Nepal.



d) The research team also suggested to reform income tax administration by including the affluent taxpayers into tax net, providing the permanent taxpayers register. (Agrawal, 1978)

Agrawal (2004) has published a book entitled, "Income Tax; theory and Practice." This book has focused on the students of chartered accountants and taxation. This book has also focused to be practitioners' reference and handbook, rather than theoretical compilation on the subject. His book is not only based on description fact but also has interrupted the various provisions of the new act. Simple and clear language has been used in this book. Sufficient theoretical concepts with clear interpretation as well as sufficient examples are included in this book. This book has depth theoretical concept and examples. Some sections of ITA 2058 act have compared with the international accounting standard. Gain or loss adjustment of depreciated assets in an example. All terms are clearly defined with sections under which the terms are included (Agrawal; 2004)

In 2001, Revenue Consultation Committee Report has studied the overall taxation situation in depth. It highly emphasized to simplify the tax policy to increase voluntary compliance. This report recommended for written communication between taxpayer and tax administration rather than the informal relation. This report suggested widening the income tax bases by including all kinds of taxpayer of new sector. For this, the report suggested to make the act more transparent and clear in order to attract foreign and domestic investors. It was further suggested to increase income tax exemption limit with considering purchasing power and inflation rate. (Revenue Consultation Committee, 2001)

Kandel (2003) had criticized the income tax act 2002 on several grounds. Exemption of agriculture from income tax, export duties levied on export, inequality between different capital earned income (i.e. tax on interest, dividend, and capital gain), and withdrawal of the provisions of exemption suddenly and no adjustment for inflation are the major issue he raised in his article. He further criticized the Act for the provision for income tax from export as 0.5 percent of total export because it is not good choice of income tax base. (Kandel, 2003)

Adhikari (2002) has discussed the legal provision of new Income Tax Act, 2002. His book is analytical rather than informative. Writer has not included administrative aspect, role and structure of income tax in his book. The book has only focused on the legal aspect of income tax. Agreement and protocol relating to avoidance of double taxation and the prevention of fiscal evasions with respect to taxes on income between different countries had also included in his book. (Adhikari, 2002)

Mallik (2003), has published book named, "Nepalese Modern Income Tax System". He described historical aspects of income tax and legal provisions relating to income tax with numerical examples. This book is very useful to know the general information and legal provision of Income Tax Act, 2002. His focus is on Income tax in Nepal, role of income tax, administrative and legal aspects of income tax in Nepal. His study is useful to find out facts and figures about the income tax in Nepal at that time.

Poudyal and Timilsina (1990) presented a book based on B.com syllabus. This book is designed to give theoretical as well as practical ideas of income tax in Nepal. Provisions and methods of assessment have been described with numerical examples but the major problems and defects of income tax system of Nepal have not been analyzed. (Poudyal and Timsina, 1990)

Khadka (1994), had discussed the economic policy of Nepal, VAT as a long term tax for Nepal, Income tax, improving tax, administration tax, tax reform strategy. He had analytically described about development, existing structure, main problems and possible direction of reform of income tax. He had indentified the major problems of income tax as narrow coverage, unscientific tax assessment and collection, defective system from the perspective of international taxation. Weak tax administration, imbalance and inadequate tax training, predominance of law level non technical posts, debatable scope of revenue investigation department, and lack of information system were the major problems of tax administration identified by him.

He had suggested some suggestions to overcome from the problems of income tax which were extension of tax coverage, scientific method of tax assessment, extension of withholding tax, inflation adjustment etc. He had also identified some

possible direction for administrative reform. They were reorganization and expansion, applying integrated information system; research unit on taxation, strengthening the revenue service. His book was analytical and very useful to obtain the various aspects of income tax. (Kahdka,1994)

Dhakal (1998), presented his extended, enlarged and modified edition of his book including value added tax. This book is mainly based on the syllabus of BBS third year. The provisions made under income tax laws and the methods of income tax assessment have been described with numerical examples. This book is more helpful to know about general information and provisions made under Income TAX Act 1974. But he has not analyzed the role of income tax, income tax structure and defects of income tax system of Nepal. His book is informative rather than analytical. (Dhakalm 1998)

In 1999, Adhikari has published a book which is mainly based on the T.U. syllable of B.B.S. third year. Apart from the theoretical concept of taxation, he has also presented the historical background, income tax laws and its implementations, assessment of tax and tax authorities, rights and duties. He has also described the management of VAT, property Tax and Sales Tax. The book includes precedents of Supreme Courts about Income Tax, classification and interpretation of revenue code, tax planning and income tax management in Nepal. The book is based in Income Tax Act, 2031. (Adhikari, 1999)

Khadka (2001), published a book on income tax of Nepal. The book contains many interesting articles on various aspects of income tax. It first traces out the evolution of income tax around the world. It then analyzes relative importance of income tax in the tax system of some selected countries. It also defines various concepts, which are widely used in the modern income tax literature. The book also reviews major changes introduced in the field of the Nepalese income tax system since its inception in 1959 AD and examines its existing structure and operation. It also analyzes the current problems and makes recommendations for the rationalization of the structure and modernization of operation of the income tax system. The book also includes income tax acts of 1959, 1962 and 1974 A.D. (Khadka, 2001)

Tiwari (1999), presented a book about income tax system in Nepal. This book is published mainly for the students of Tribhuvan University but it is equally useful to the tax payers, tax administrators and those who desire to get theoretical as well as practical knowledge about income tax. He has described the provisions under Income Tax Act 1974, income tax rules, information and acts related to income tax etc. He has not analyzed the major problems of income tax system (Tiwari, 1999)

## **2.20 Review of Dissertation**

Gautam has presented a dissertation entitled, "Contribution of income tax to the national revenue of Nepal" . He has studied the contribution of various taxes in the government revenue, tax revenue, GDP. According to his the contribution of tax revenue in the government revenue is 85.2% in the income year 1982/83 and decreased to 78.0% in the income year 2001/02. Nepalese income tax revenue is the composition of income tax from the public enterprisers, semi public enterprises, private corporate bodies, individuals, remuneration and tax on interest. Income tax of Rs. 8903.7 millions was collected in 2001/02. Share of individuals to income tax revenue is the highest. Within income tax, there is dominant role of individuals and it is decreasing trend which was 69.63% of income tax revenue in 1982/83 but decreased to 49.63% of income tax in year 2001/02. The contribution of individual income tax is in first position; Income tax exemption limit in Nepal was Rs. 70000 for all taxpayers in 1959/60 but at present income tax exemption limit is 80000 for individuals and Rs. 100000 for couples and family in 2003/04. The exemption limit is not provided for partnership firms, corporation and non residents. It is found that exemption limit has been changed on the need of time and income.

Personal income tax rate was 5 to 50 percent with 7 slabs in 1980/81 but at present (i.e. for 2003/04) it is reduced to 2 slabs. In the same way, corporate tax rate was 10 to 55 percent with 1980/81 but at present taxpayers are taxed at flat rate. Income tax is 15 percent and 25 percent for personal income tax over exemption limit, 30 percent for bank, finance companies and 25 percent for other corporate taxpayers.

His suggestions are that the objectives of taxation should be growth redistribution, and stabilization of economy. So, the income tax policy should be properly formulated on the basis of critical analysis of existing situation (Gautam, 2004)

Kayastha (1974) has tried to analyze the contribution of income tax and property taxes to overall revenue generation in Nepal. He has studied on legal and administrative aspect income tax system of Nepal and pointed out some drawback. According to him before 1951, Nepal didn't have scientific economic policy, which could facilitate the economic development of the country. According to him, the major problems of income tax system of Nepal are income tax evasion at high level and greater role of indirect tax in tax revenue. These problems have not solved yet effectively. (Kayastha, 1974)

Pandey (1978), in his study has discussed various aspects of incomes tax such as legal aspects, structure of income tax role of income tax, problems of income taxation, economic effect on income tax in Nepal. He had highlighted on tax structure of Nepal. According to him, income tax played as significant role in the economic development of Nepal. He found the capital burden of income tax was Rs. 0.2 in 1962/63 and it had increased to Rs. 7 in 1975/76. He had stated that indirect tax had a dominated role in the total tax revenue. Lack of scientific record keeping, Lack of maintaining accounts by tax payers, lack of co-ordination, lack of honest tax officers are the major problems identified by him. His suggestions about income tax were capital gain should bring in tax net; income tax accounting assessment and collection method must be scientific etc. His study was done with objectives of examining the economic effects of income tax but he had not described it with numerical examples and empirical investigation. (Pandey, 1978)

Subedi (1982) has analyzed about the role of income tax on national revenue of Nepal. he has examined the growth of income tax collection, its ratio to GDP cost of income tax collection and elasticity. He has also included historical perspective and legal aspect of income tax in his study. He has pointed out that tax evasion, insufficient tax administration and dominated role of indirect tax are the major problems in Nepalese tax system. He has suggested that tax administrative reform is the major necessity in development of income tax system. (Subedi 1982)

Nepal (1983), has critically examined the income tax system of Nepal in that time. Her study has been conducted with purpose of examining the role of income tax in overall tax structure, analyzing the problems and prospects of income tax in Nepal and highlights the future prospective of the Nepalese income tax (Nepal, 1983)

Regmi (1986) has prepared a dissertation with the main objective of examining the trend of income tax in Nepal, ascertaining the share of income tax to total tax revenue and its ratio of gross domestic product. He has also stated as a great problem in income tax in Nepal. To increase the revenue of government, he has recommended that income tax should be clear and precise, scientific method for accounting assessment and collection of income tax, widening tax coverage, easy and simple procedure of tax payment, public awareness. (Regemi, 1986)

Bhandari (1994) has tried to examine historical background, tax structure in Nepal and contribution of income tax to economic development of Nepal. He has stated that actual collection of revenue through income tax was lower than its estimated targets because the poor tax paying habit of Nepalese tax payer, poor tax administration system, wide spread evasion of income tax. He has suggested to make effective personnel management, increasing habit of tax paying of Nepalese tax payer through proper education and better public communication system, maximize tax evasion, reduce tax collection cost. (Bhandari, 1994)

Acharya (1994) has mentioned the main objective of income tax as to achieve social justice, to check inflation and to collect more government revenue. He has identified the contribution of individual in total income tax revenue seems to be greatest during his study period followed by public enterprises, enumeration, house rent, and interest taxes, semi public, enterprises and private corporate bodies respectively. He has also analyzed the administrative and legal aspects of income tax. He has recommended simplifying the tax structure, legal and administrative aspect, and understanding with the consent of tax payer to raise income tax revenue. (Acharya, 1994)

Shahu (1995) has found that 0.35 percent of total population came under the category of taxpayer during his study period. Main objectives of his study was to study Nepalese structure, role and contribution of income tax on national revenue. He has

identified that income tax has been gradually increasing and was in the fourth place in the tax structure of Nepal. He has not discussed the major aspects of income tax clearly and analytically so it is incomplete study and all things mentioned in it are not also fully relevant today because it was made 9 years ago. (Shahu, 1995)

Shakya (1995) presented a dissertation named "Income Tax System in Tax structure of Nepal." His study was done with basic objective of analyzing the cause of heavy reliance of indirect taxes, analyzing the volume of indirect tax revenue and direct tax revenue in total structure, highlighting the revenue assessment procedure from different sources and suggesting improving on them. In his study, he has identified the income tax has occupied fourth position among tax revenue in Nepal. Custom duty, sales tax and excise duty has occupied first, second and third position respectively in Nepalese tax revenue. He has mentioned Nepalese taxable capacity is limited by various factor such as low per capita income, extensive subsistence economy, relatively "closed" (India) economy, weak export position etc.

He found the ratio of income tax to GDP total revenue; total tax revenue and direct tax revenue have been on increasing trend in Nepal. But increasing trend rate is very low in comparison to other countries. Tax evasion is the main reason behind it. Lack of clear and comprehensive definition of income, lack of punishment to the evaders, low tax paying capacity and non conscious of taxpayers, lack of inefficient tax administration, lack of scientific method of tax collection and lack of trained tax collectors were the main reasons of income tax evasion identified by him. (Shakya, (1995)

Shrestha (2001), study had covered the historical background, legal provisions, structure of income tax, income tax administration in Nepal and empirical investigation. Her findings about tax structure were: there was dominant share of tax revenue in Nepalese government revenue. But the contribution of tax revenue showed the decreasing trend. The tax / GDP ratio was not found satisfactory with compare to other SAARC countries. It was 6.81 percent for the period of 1984/85 and 9.36 percent in 1998/99. There was serious and growing financial resource gap in Nepal seems to be never ending problem for Nepalese economy. There was dominant role of indirect tax revenue in Nepalese tax revenue. The contribution from individuals to income tax

revenue was 17.76 percent and 82.24 percent respectively in 1984/85 which becomes 26.14 and 73.86 percent in 1998/99. The contribution from individuals to income tax revenue was greatest in every fiscal year and it was increasing trend. Income tax revenue was playing a significant role in direct tax revenue because the share of income tax in direct tax was increasing rapidly.

She had found various problems of income tax system in Nepal. They were Narrow tax coverage, mass poverty of Nepalese people, and lack of conscious of taxpayer, widespread evasion and avoidance of income tax, unscientific tax assessment procedure, inefficient tax administration, complicated tax laws and procedures, instability in government policy. She had also identified the major weak points of income tax administration in Nepal. They were failure to locate new taxpayers, failure to maintain proper accounts and records, defective selection of personnel, undue delay in making assessment, lack of motivation in tax personnel, existence of corruption.

She had also suggested broadening the Nepalese income tax base by bringing agriculture income and capital gain under income tax net. She had suggested to make consciousness to people, reform of income tax assessment, reform the tax administration and minimizing the tax evasion. For the improvement of income tax administration, she had suggested computerization and effective exchange of information, tax education to tax payers, tax inspectors and officials, effective personnel management, Her suggestion for minimizing tax evasion were control illegal business activities, enforce proper auditing and investigation, enforce heavy fines and penalties and maintain proper records and accounts. (Shrestha, 2001)

Pradhan (2002), study is basically concerned with historical background, contribution of income tax to the public revenue, contribution of Nepal Telecommunication Corporation (NTC) to income tax, effectiveness of income tax collection. She had found the contribution of income tax from public enterprises in Nepal was not significant due to poor achievement, weakness in government's economic policy and deficiency in legislation. NTC has been controlling effectively to total income tax revenue. Contribution of tax revenue on GDP of Nepal was lower than other SAARC countries except Bangladesh. Average contribution of income tax from NTC to



total tax revenue, total income tax revenue and total government revenue was 2.37 percent, 15.60 percent and 1.93 percent in her study period.

Her suggestion about income tax system were clear cut provision, discretionary power of tax officers should curtailed, assessment and collection provision should be made clear and simple, provision of reward, prize, incentive should introduce to encourage the taxpayer to pay voluntarily, compulsorily provision of auditing, etc. For the improvement income tax administration in Nepal, she had suggested promotion and rewards to active, efficient and honest tax personnel, tax education to tax payers, strict actions against corruption, and reduction of delays in tax assessment. Specially, her study had focused on the study on Nepal Telecommunication Corporation. (Pradhan, 2002)

Sherchan (2003), study had covered tax structure, role of income tax and legal provision of income tax. But specially, his study has focused on provision of fines and penalties. He had found that there were dominated share of tax revenue in Nepalese government structure. Income tax had occupied third position in his study period and it as increasing trend. The tax /GDP ratio was not found satisfactory. With the income tax, there was the dominated role of corporate income tax but it was in decreasing trend and contribution of individual income tax was second position and it was in increasing trend.

He had suggested to revise the position of fees and penalties, introducing reward, prize, incentives position, clear income tax, rules and regulation, clear right and duties of tax officers. Further, his suggestions were: timely revision in income tax policy, computerized system for payment of income tax. This study was done with main objective of analyzing tax structure of Nepal, analyzing the position of fines and penalties under income tax law, know the taxpayers knowledge and tax officers view about fines and penalties. His study had focused only on provision of fines and penalties. So, this study is incomplete study. (Sherchan, 2003)

Palli Magar (2003) had covered tax structure role of income tax and exemptions and deduction provided in the law. He had found that there was dominated share of tax structure in Nepalese government revenue. Income tax had occupied third position in his study period and it was in increasing trend. The tax/ GDP ratio was not found satisfactory. With the income tax, there was the dominated role of corporate income tax

but it was in decreasing trend and contribution of individual income tax was second position and it was in increasing trend. Lack of employees, shortage of income tax experts professionals in tax administration, lack of public participation, faulty organizational structure of tax administration, weakness in government policy, defective income tax act were the major cause for inefficient tax administration, observed by him. His suggestion about exemption were: revision the exemption limit, elimination double taxation on dividend, tax rebate for submitting true income statement in time, increase income tax rate slab up to 10, increase the exemption limit to individual as well as family etc. Besides above, suggestions about deduction were: clear provisions for improvement expenses, research and development expenses. He is totally concentrated on the exemption and deduction in his study. He has not studied about various aspects of income tax. (Palli Magar, 2003)

Besides these reports, books and master level dissertations, some articles about income tax published in Kathmandu Post, Rising Nepal, Gorkhapatra, The Kantipur, The Kathmandu Post etc. and publication of Ministry of Finance such as Budget speech, Economic Survey were reviewed in the study period.

Shrestha (2006) has tried to show the contribution of income tax on the structure of government revenue in Nepal. She stated that the composition of tax and non tax revenue is still less satisfactory in Nepal. She found that total revenue, total tax revenue and direct tax revenue have an increasing trend in Nepal but in low rate. She has mentioned that tax evasion as the major problems of income tax system in Nepal in her study, inefficient administration, unconsciousness of tax payer, lack of scientific method of tax assessment and collection have identified as the major reasons for tax evasions at high level. (Shrestha, Neena 2006)

Siwakoti (1987) has explained the various aspects of income tax. His study emphasized on drawing a clear sketch of role of income tax, structure of income tax, projection of income tax, legal aspect of income tax act and problems of income tax. Major problems existing in Nepalese income tax system, stated by him are narrow coverage, unscientific and time consuming assessment and collection procedure, complicated act and defective income tax act. (Siwakoti, 1987)

Baral (1989), has tried to show the contribution of income tax on the structure of government revenue in Nepal. She stated that the composition of tax and non tax revenue is still less satisfactory in Nepal. She found that total revenue, total tax revenue and direct tax revenue have an increasing trend in Nepal but in low rate. She has mentioned that tax evasion as the major problem of income tax system. In her study, inefficient tax administration, unconsciousness of tax payer, lack of scientific method of tax assessment and collection have identified as the major reasons for tax evasion at high level. (Baral, 1989)

Akhanda Shrestha(2009) has tried to show the revenue collection from income tax and its practical difficulties in Nepal. In his thesis he has written that the revenue collection from income tax is in increasing trend. He has also explained the revenue collection from income tax of different years. He has also stated various practical difficulties of income tax. To remove the practical difficulties of income tax, he has given suggestions to the government. Some of his suggestions are as follows:

- a) Income tax policy should be formulated according to the economic policy
- b) It should be revised timely.
- c) The members involved in formulating income tax policies must have depth knowledge about income tax.
- d) Tax should be increased gradually on long term basis to meet the deficit in the budget. For this tax base should be widened.
- e) There must be co-ordination between the departments of tax and so on.

## **2.21 Research gap**

Tax is the strong sources of government revenue. It plays important role in revenue collection. To increase the revenue collection from tax the government should either increase the tax to make wide coverage. If tax collection is effective the government revenue will increase well. Tax system depends on its legal provision and

its popularity also depends on its transparency for providing a lot of information about tax. Different researches have research on the topics of income tax in different ways. Their objectives and analyzing system are in different way. After studying different research paper held on “Contribution of Income tax in total revenue of Nepal ” , the researcher found various gap on selected topic to make this research different for other research also analyze theoretical concepts. Analyze the reliable data and analyze the different views of different respondents.

## **Chapter – 3**

### **RESEARCH METHODOLOGY**

The chapter ‘Research Methodology’ is devoted to the research methods applied in the study for the achievement for desired objectives. The both primary as well as secondary sources of data are used to conduct this study. Opinion survey technique was adopted while collecting primary data to find out the views of respondents representing different groups related to income tax. This opinion survey was adopted to find out the practical aspect of income tax. While conducting the opinion survey, questionnaires were distributed to the tax experts, tax officers, businessmen and consumers in the sizeable manner in Janakpur municipality.

#### **3.1 Research Design**

To get the stated objectives of the study, the study of income tax act 2058 made descriptive research where as analytical research has been carried out in terms of role of vat in generating government revenue in Nepal, for an empirical research, an opinion survey has been conducted. The opinions of various seventy-five respondents, tax experts and tax payers were collected through structured questionnaire with references to tax system of Nepal, major problem of tax system, remedy to minimize corrupt practice existed in Nepalese tax administration, cause of ineffectiveness of tax administration, the most important factor for effectiveness of tax including necessary suggestion for achieving effectiveness of tax in Nepal. Hence, the research methodology followed in the study can be termed as survey cum analytical and descriptive research design.

#### **3.2 Population and Sample**

In order to benefit this study 75-sample size from Janakpur is selected. Persons included in the sample are carefully selected by consultation with tax experts, professor and judgment of the researcher. They have been divided into three groups. The under given table shows the group of respondents and the size samples.

**Table No. 3.1**  
**Groups of Respondents and size of samples from each group**

Serial Number	Group of respondents	Sample Size	%
1.	Tax expert	25	33.33
2.	Tax administration	25	33.33
3.	Tax payers	25	33.33
	Total	75	100

### **3.3 Source of Data**

Both primary as well as secondary sources of data have been collected in order to achieve the real and fact full result from this research. All the possible and useful data as far available have been collected. The major sources of data as follows:

#### **a) Primary data**

Distribution of questionnaires to responsive of persons is the major tools used for the collection of primary data. A set of questionnaire was developed and distributed to the selected respondents in order to get accurate and actual information. The questionnaire was distributed to different tax group i.e. tax experts, tax administrations and tax payers. Tax experts and tax officers are selected from tax department, various sectors of tax officers in Janakpur municipality, reputed lawyer, auditors and intellectuals who have knowledge and ideas about tax. Tax payers i.e. business-men and consumers are selected form different manufacturing company trading company, department stores, shopping center, finance company etc.

## **b) Secondary data**

The secondary sources of data are the information services from books, journals, newspapers, reports and dissertations etc. The major sources of secondary data are from the economic survey and annual report, Ministry of Finance publications, Tribhuvan University, reports and records of department of taxation. Ministry of Finance, dissertation related to tax available at library of R.R.M.Campus Janakpur, central library of TU, Publication of tax projects, publication of tax department, economic review and indicators from Nepal Rastra Bank, world development report, published documents of Nepal Rastra Bank and national planning commission, books related to tax, national news paper, Journals, souvenir and news magazines, other relevant records and data related to his studies.

### **3.4 Data collection Procedure**

A total 75 sets of questionnaire were distributed to the selected respondents in order to get actual and accurate information. Distribution work is done personally rather than sending by any means to get accurate and actual information in time.

### **3.5 Data Processing and analysis Procedure**

The information revived from primary and secondary sources is firstly tabulated in to separate formats systematically in order to achieve desire objectives. After that these data are tabulated and analyzed for the purpose of analysis generally simple statistical tools have used which are simple percentage methods, ranking methods, graphs, charts and diagrams.

## Chapter-4

### DATA PRESENTATION AND ANALYSIS

#### 4.1 Analysis of Secondary Data:

##### 4.1.1 Revenue collection from tax

Tax revenue is the main source of government revenue. Revenue collection from tax is in increasing trend. The revenue collection from tax in fiscal year 2000/01 is Rs. 38865.1 million but in FY 2007/08 the revenue collection is Rs85155.54 million it shows the revenue collection from tax is increasing trend. Following table shows the revenue collection from tax in different year. Tax revenue included customs, tax on consumption and product of goods and services land revenue and registration and tax on property profit and income. The total tax collection during the seven year has given in the table below.

**Table No. 4.1**  
**Revenue collection from tax**

Rs. in million

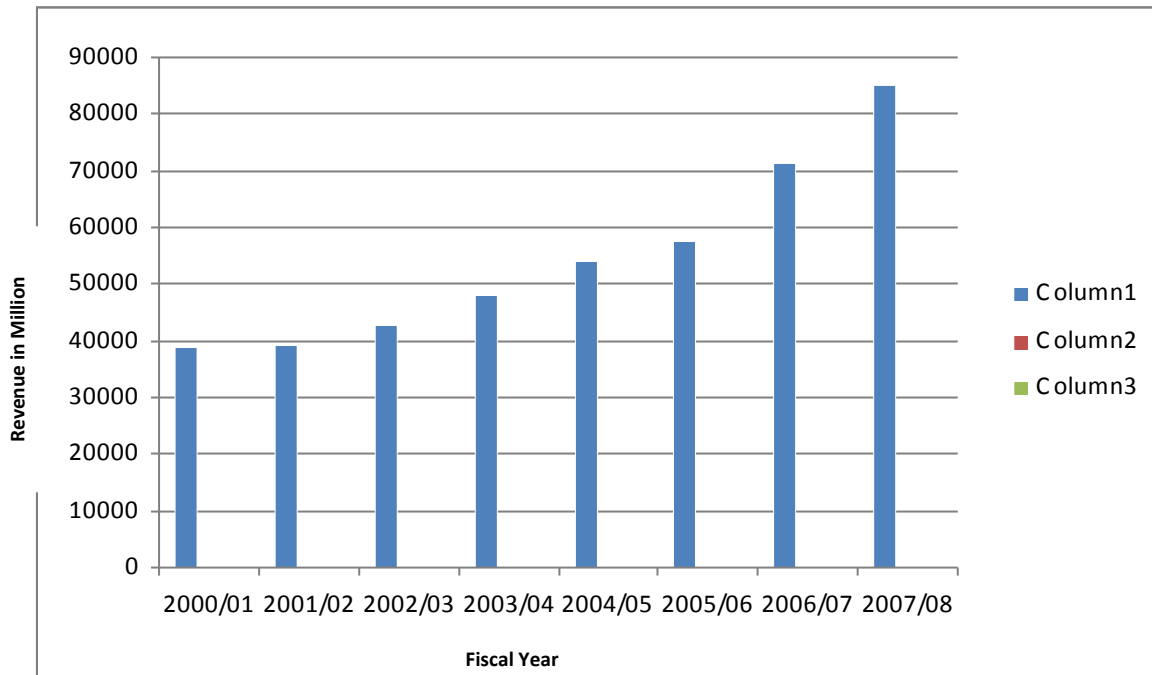
<b>Fiscal Year</b>	<b>Tax Revenue</b>
2000/01	38865.1
2001/02	39330.6
2002/03	42587.0
2003/04	48173.0
2004/05	54104.7
2005/06	57430.4
2006/07	71126.7
2007/08	85155.54

Source: Economic Survey 2008/09 MOF.



From the above table the tax revenue was increased from FY 2000/01 to 2007/08. The above explanation can be shown in following figure.

**Figure No. 4.1**  
**Revenue collection from tax**



#### 4.1.2 Composition of tax revenue

Tax revenue includes the tax from customs, tax on consumption and product of goods and services land revenue registration, tax on property profit & income. The composition of tax revenue of different year has given in following table.

**Table No. 4.2**  
**Composition of tax revenue**

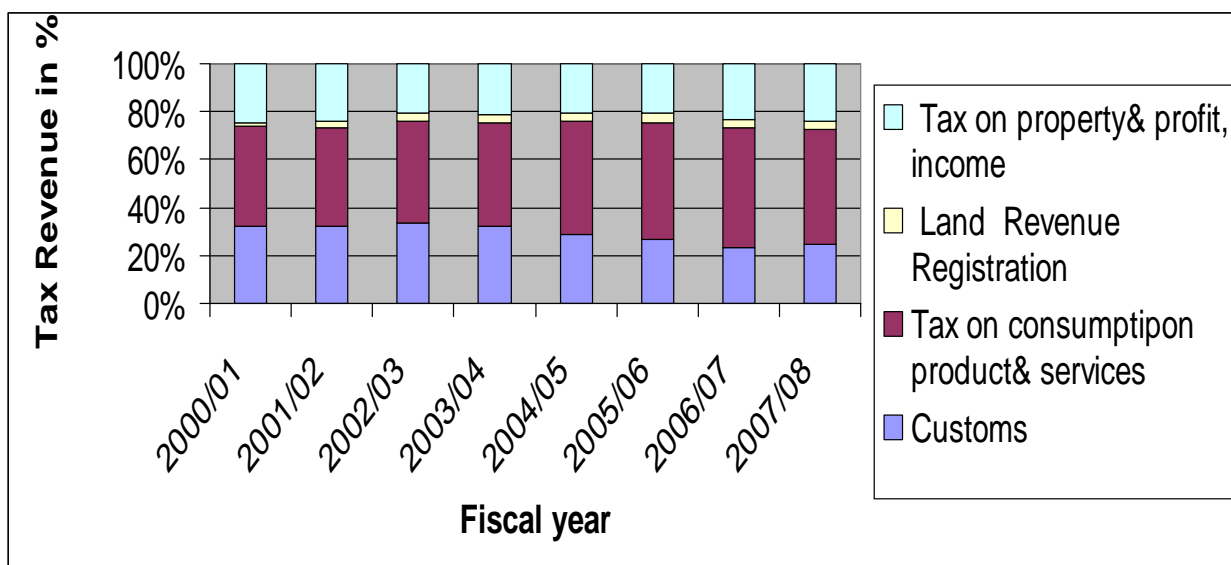
Rs. in Million

Fiscal year	Customs	Tax on consumption and Product of goods services	Land revenue registration	Tax on property profit & income	Total
2000/01	12552.1	16153.6	612.9	9546.5	38865.1
2001/02	12658.8	16074.3	1131.8	9465.7	39330.6
2002/03	14236.4	18244.8	1414.3	8691.5	42587.0
2003/04	15554.8	20705.6	1697.5	10215.1	48173.0
2004/05	15701.6	25331.3	1799.2	11272.6	54104.7
2005/06	15344.0	28118.3	2181.8	11787.0	57430.4
2006/07	16707.6	35433.8	2253.5	16726.8	71126.7
2007/08	21062.5	41005.32	2940.74	20147.02	85155.54

Source: Economic survey 2008/09, MOF.

Tax revenue is the major sources of government revenue in Nepal. In the tax revenue the major sources of tax is custom tax. It includes imports, exports, Indian excise returned and others. Another major source of tax is tax on consumption goods and services. It includes exercise on industrial product and value added tax. Another source of tax is income tax .It includes tax from public enterprises, semi-public enterprises, private corporate bodies and individuals. Tax from remuneration, House and land tax, Vehicle tax, tax on interest and others. The tax collection from different year in different year is shown in above table which shows the every sources of tax is in increasing trend the above data can be shown in following figure.

**Figure No. 4.2**  
**Composition of tax revenue**



#### 4.1.3 Composition of tax revenue & non tax revenue

Tax revenue includes tax from customs, tax on consumption and production of goods and services, land revenue registration and tax on property, profit and incomes. Non tax revenue includes charges, fees, fines and forfeiture, receipts from sale of commodities and services, dividend, royalty and sale of fixed assets, principal and interest payment and miscellaneous. The composition of tax revenue and non tax revenue of government in different year has given in following table:-

**Table No. 4.3****Composition of tax revenue and non tax revenue**

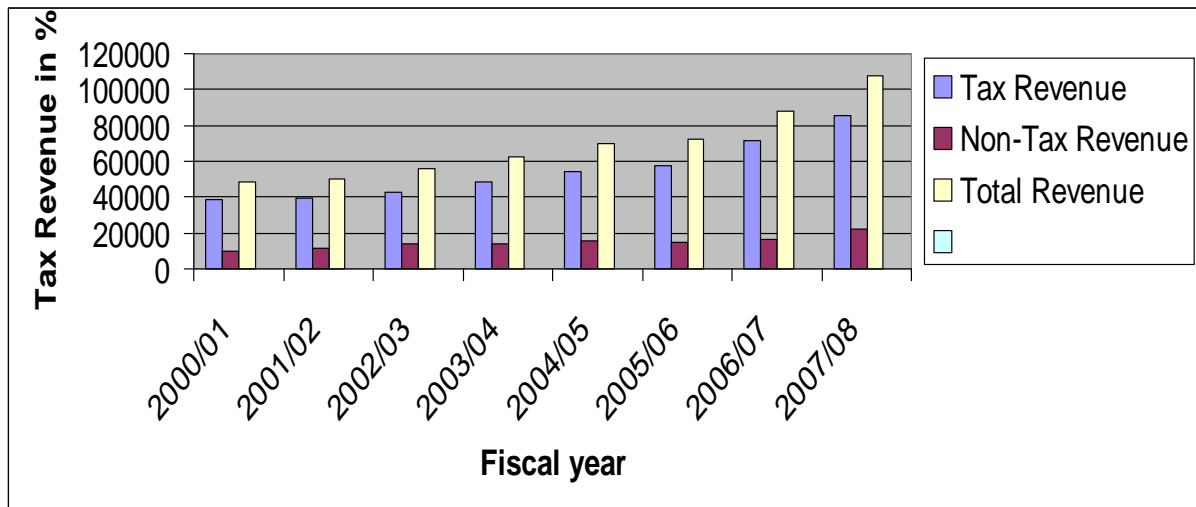
Rs. in million

Fiscal year	Tax revenue	Non tax revenue	Total revenue
2000/01	38865.1	10028.8	48893.6
2001/02	39330.6	11115.0	50445.5
2002/03	42587.0	13642.7	56229.8
2003/04	48173.0	14158.0	62331.0
2004/05	54104.7	16018.0	70122.7
2005/06	57430.4	14851.7	72282.1
2006/07	71126.7	16585.8	87712.10
2007/08	85155.54	22467.04	107622.58

Sources: Economic Survey 2008/09, MOF.

From the above table it is clear that the major part of total revenue is tax revenue. The revenue from tax in year 2000/01 was Rs. 38865.1 million and from non tax revenue was 10028.8 million. Similarly the revenue from tax in fiscal year 2001/02, 2002/03, 2003/04, 2004/05, 2005/06, 2006/07 and 2007/08 are Rs. 39330.6, Rs. 42587.6, Rs. 48173.0, Rs. 54104.7, Rs. 507430.4, Rs. 71126.7 and Rs. 85155.54 million respectively. Similarly revenue collection from non tax was in fiscal year 2001/02, 2002/03, 2003/04, 2004/05, 2005/06, 2006/07 and 2007/08 were 11115.0 million, Rs. 13642.7 million, Rs. 14158.0 million, Rs. 16018.0 million, Rs. 14851.7 million, Rs. 16585.5 and Rs. 22467.04 million respectively. This explanation has been shown in following figure.

**Figure No. 4.3**  
**Composition of tax and non tax revenue**



#### 4.1.4 Revenue collection from Income Tax

The main source of tax revenue of government is income tax. Income tax includes corporate tax, individual tax and interest tax. Corporate tax includes Income tax from Public Enterprises, Income tax from Semi-public Enterprises and Income tax from Private Corporate bodies. Individual tax includes income tax from Individual and Income tax from remuneration, Interest tax related to Interest Income.

In the fiscal year 2000/01 revenue collection from Income tax was Rs. 9114.0 millions and in Fiscal year 2007/08 revenue from Income tax is increased up to Rs. 17311.22 Millions. The following table shows the revenue collection from Income tax in different year.

**Table No. 4.4**  
**Revenue collection from Income tax**

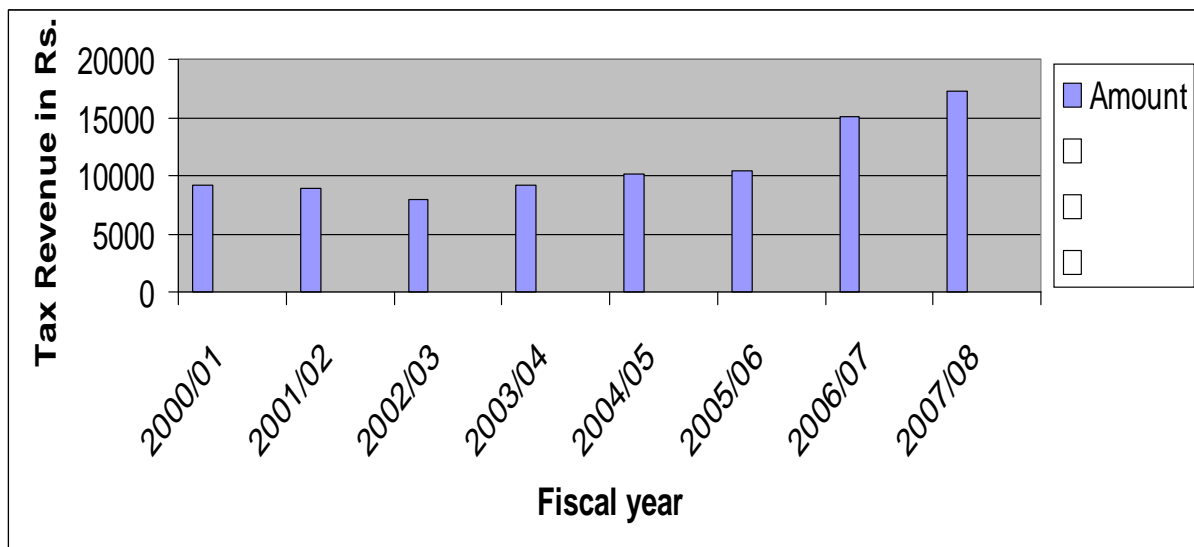
Rs. in million

<b>Fiscal Year</b>	<b>Amount</b>
2000/01	9114.0
2001/02	8903.7
2002/03	7966.2
2003/04	9245.9
2004/05	10159.4
2005/06	10373.7
2006/07	15034.0
2007/08	17311.22

Source: Economic Survey 2008/09 MOF.

The trend of revenue collection from Income tax can be shown in following figure.

**Figure No. 4.4**  
**Revenue Collection from Income tax**



#### 4.1.5 Composition of Income Tax

Income tax includes corporate tax, and Individual tax and Interest tax. Corporate tax includes Income tax from public enterprises, income tax from semi-public enterprises and income tax private corporate bodies. Individual tax includes income tax from individual and Income tax from remuneration, Interest tax includes tax related to Interest Income.

The composition of Income Tax in different year is given in following table:-

**Table No. 4.5**  
**Composition of Income tax**

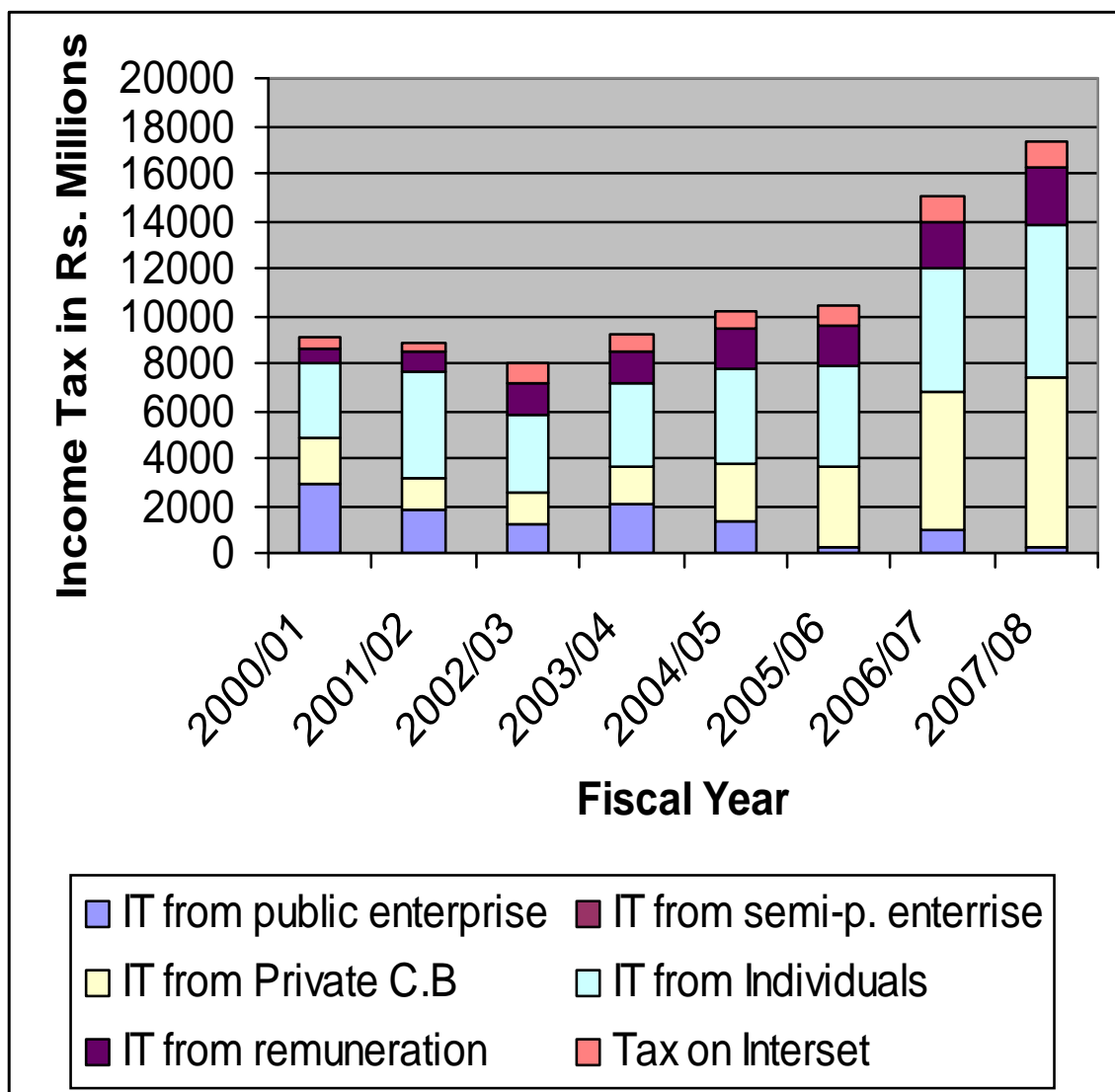
Rs. in million

S.N.	Heading / Fiscal Year	2000/01	2001/02	2002/03	2003/04	2004/05	2005/06	2006/07	2007/08
1.	Income tax from public Enterprises	2928.0	1769.3	1251.0	2056.0	1332.4	195.7	1019.7	204.58
2.	Income tax from semi-public Enterprises	0.0	0.0	0.0	0.0	0.0	0.0	0.0	00
3.	Income tax from Private Corporate Bodies	1924.3	1412.0	1236.3	1531.3	2467.8	3404.3	5717.1	7186.46
4.	Income tax from Individuals	3200.5	4419.1	3362.3	3533.4	3926.3	4234.7	5234.4	6381.21
5.	Income tax from Remuneration	597.3	835.6	1252.6	1391.2	1675.9	1764.1	2007.9	2491.04
6.	Tax on Interest	463.9	467.7	864.0	733.4	757.0	774.9	1054.9	1087.93
	<b>Total</b>	<b>9114.0</b>	<b>8903.7</b>	<b>7966.2</b>	<b>9245.9</b>	<b>10159.4</b>	<b>10373.7</b>	<b>15034.0</b>	<b>17311.22</b>

Source: Economic Survey 2008/09, MOF.

The above table shows the composition of income tax revenue in different fiscal year. The above explanation has been shown in the following figure which shows the composition of income tax revenue in different fiscal year.

**Figure No. 4.5**  
**Composition of Income tax revenue**





#### 4.1.6 Contribution of Income tax to Total Revenue of Nepal

The government total revenue includes tax revenue and non tax revenue. Tax revenue includes tax from customs, tax on consumption and products of goods and services, tax from land revenue and registration, tax on property profit & incomes. Similarly non tax revenue includes charges, fees, fines and forfeitures, receipt from sales of commodities and services, dividend, royalty and sales of fixed assets, principle and interest payment and miscellaneous items. Income tax is one part of total revenue. The contribution of Income tax on the Total revenue in different year has given below:

**Table No. 4.6**  
**Contribution of Income tax in to Total revenue**

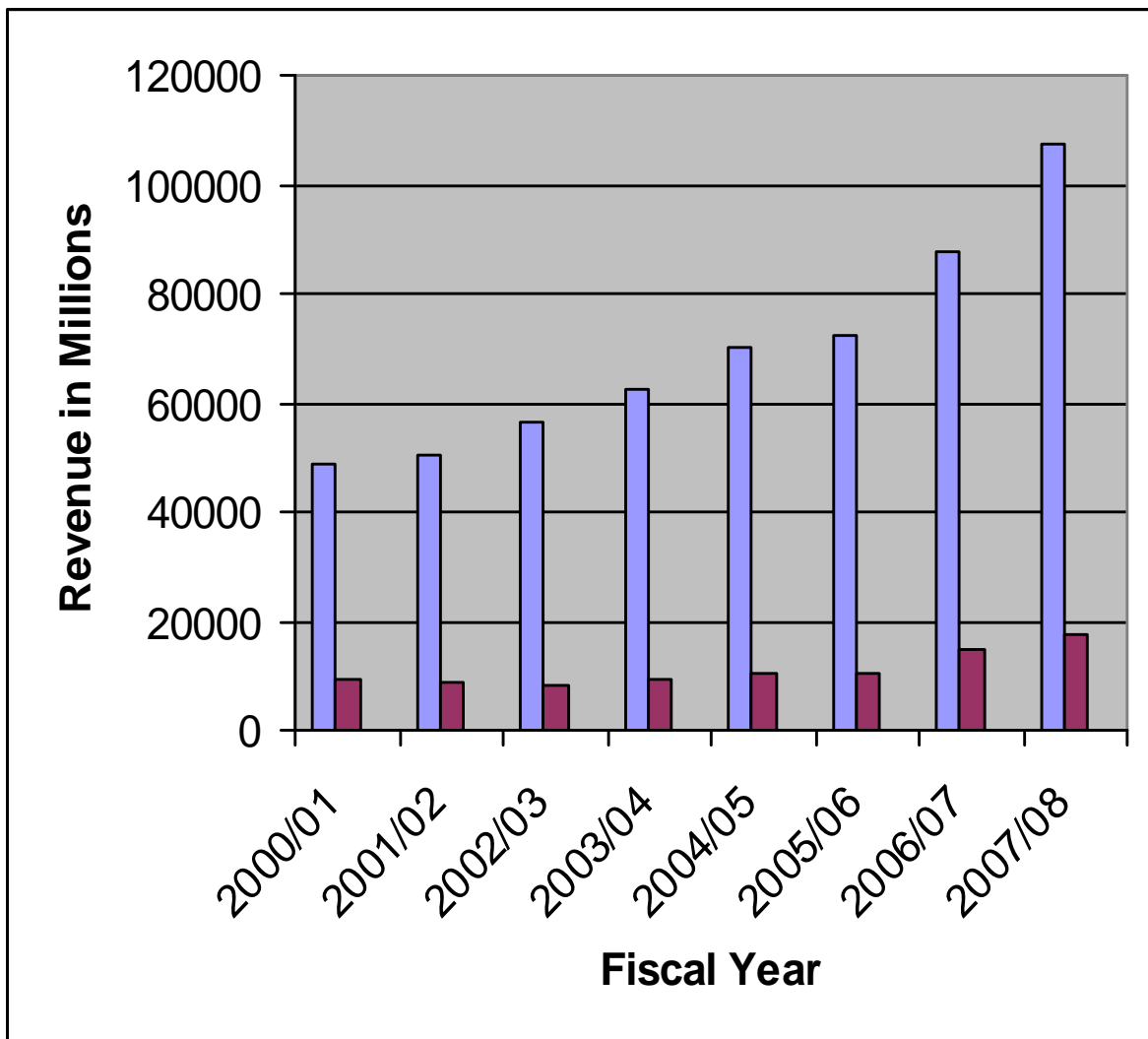
Rs. in million

Fiscal Year	Total Revenue	Income Tax	% of Income tax to Total Revenue
2000/01	48893.9	9114.0	18.64
2001/02	50445.6	8903.7	17.65
2002/03	56229.7	7966.2	14.17
2003/04	62331.0	9245.9	14.83
2004/05	70122.7	10159.4	14.49
2005/06	72282.1	10373.7	14.35
2006/07	87712.1	15034.0	17.14
2007/08	107622.58	17311.22	16.09

Source: Economic Survey 2008/09, MOF.

In Fiscal year 2000/01; the contribution of Income tax to total revenue was 18.64. Similarly in fiscal year 2001/02; fiscal year 2002/03; fiscal year 2003/04; fiscal year 2004/05; fiscal year 2005/06; fiscal year 2006/07 and 2007/08 were 17.65%, 14.17%, 14.83%, 14.49%, 14.35% , 17.14% and 16.09 % respectively. Above table shows in an average the contribution of income tax in total revenue is 15.92%. The explanation can be shown in following figure.

**Figure No. 4.6**  
**Contribution of Income tax to Total Revenue**



#### 4.1.7 Contribution of Income tax to Total tax revenue

Total tax revenue includes tax from customs, tax on consumption and products of goods and services, tax from land revenue and registration, tax on property profit & incomes. So, income tax is one of the components of total tax revenue. The contribution of Income tax on the Total tax revenue is in average 20.28%. The following table shows the contribution of Income tax to total tax revenue in different year.

**Table No. 4.7**

#### **Contribution of Income tax to Total tax revenue**

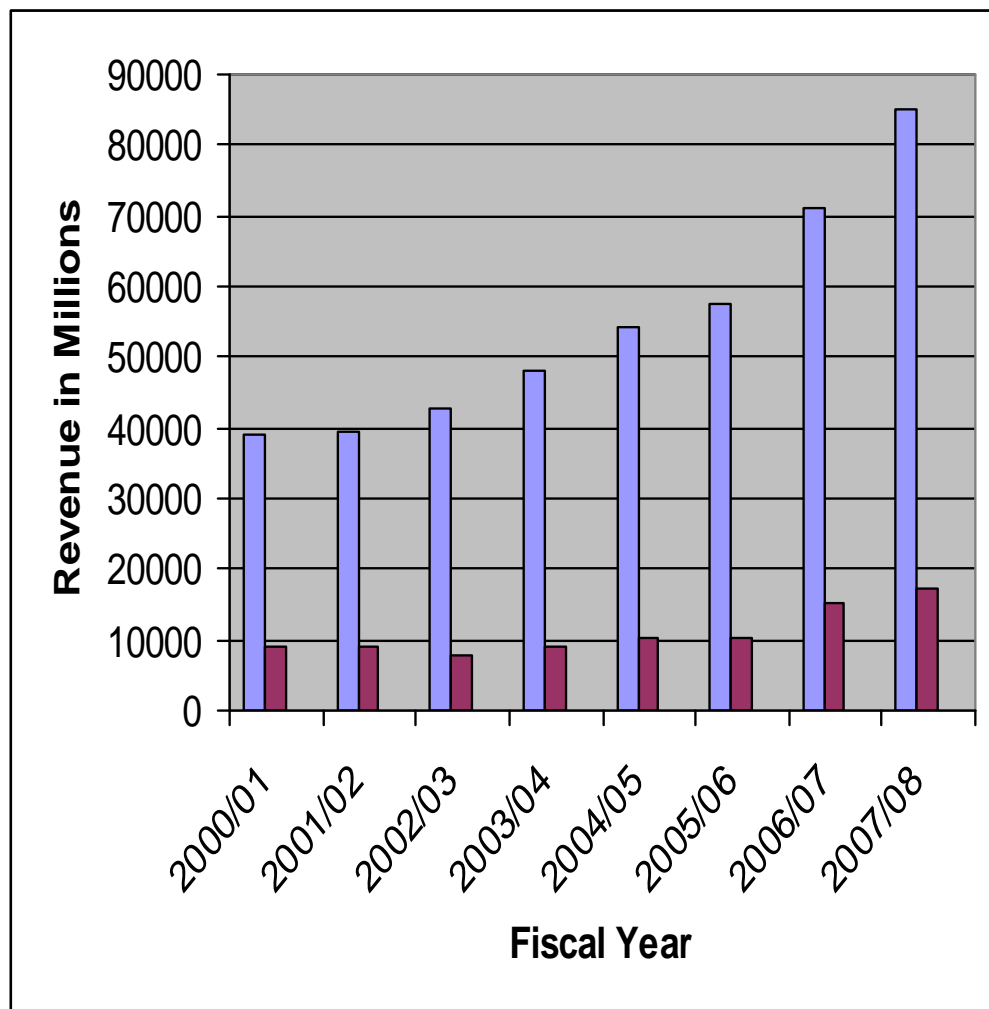
Rs. in million

Fiscal Year	Total Tax Revenue	Income Tax	% of Income tax to Total Tax Revenue
2000/01	38865.1	9114.0	23.45
2001/02	39330.6	8903.7	22.64
2002/03	42587.0	7966.2	18.71
2003/04	48173.0	9245.9	19.19
2004/05	54104.7	10159.4	18.78
2005/06	57430.4	10373.7	18.06
2006/07	71126.7	15034.0	21.14
2007/08	85155.54	17311.22	20.33

Source: Economic Survey 2008/09, MOF.

In Fiscal year 2000/01; the contribution of Income tax to total tax revenue was 23.45%. Similarly in fiscal year 2001/02; fiscal year 2002/03; fiscal year 2003/04; fiscal year 2004/05; fiscal year 2005/06; fiscal year 2006/07 were 22.64%, 18.71%, 19.19%, 18.78%, 18.06% and 21.14% respectively. Above table shows in an aggregate the contribution of income tax on total tax revenue is 20.29%. The explanation has been shown in following figure.

**Figure No. 4.7**  
**Contribution of Income tax to Total tax revenue**



#### 4.1.8 Contribution of Income tax to Direct tax revenue

Direct tax revenue includes tax from land revenue, house and land registration fees and tax on property, profit & incomes. So, income tax is one of the components of Direct tax revenue. The contribution of income tax on the direct tax revenue is in average 79.54%. The following table shows the contribution of Income tax to total tax revenue in different year.

**Table No. 4.8**

#### **Contribution of Income tax to Direct tax revenue**

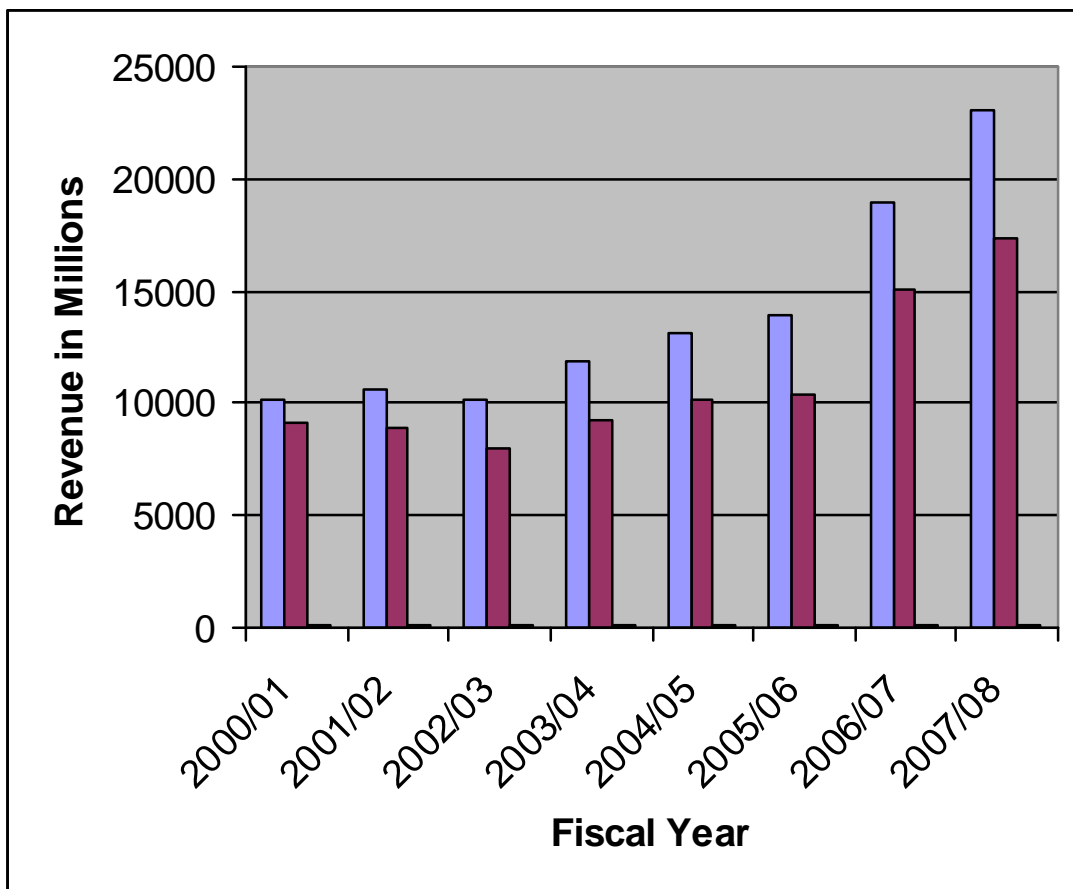
Rs. in million

Fiscal Year	Direct Tax Revenue	Income Tax	% of Income tax to Direct Tax Revenue
2000/01	10159.4	9114.0	89.71
2001/02	10597.5	8903.7	84.02
2002/03	10105.8	7966.2	78.83
2003/04	11912.6	9245.9	77.61
2004/05	13071.8	10159.4	77.72
2005/06	13968.1	10373.7	74.27
2006/07	18980.3	15034.0	79.21
2007/08	23087.76	17311.22	74.98

Source: Economic Survey 2008/09, MOF.

In Fiscal year 2000/01; the contribution of Income tax to Direct tax revenue was 89.71%. Similarly in fiscal year 2001/02; fiscal year 2002/03; fiscal year 2003/04; fiscal year 2004/05; fiscal year 2005/06; fiscal year 2006/07 and 2007/08 were 84.02%, 78.83%, 77.61%, 77.72%, 74.27% , 79.21% and 74.98% respectively. Above table shows in an aggregate the contribution of income tax on total tax revenue is 79.54%. The explanation can be shown in following figure.

**Figure No. 4.8**  
**Contribution of Income tax to Direct tax revenue**



#### 4.1.9 Government expenditure

Government expenditure includes the recurrent expenditure, capital expenditure and principal payment. In the fiscal year 2000/01 the total government expenditure is Rs. 79855.1 million which includes recurrent expenditure Rs. 45837.3 million, Capital expenditure is Rs. 28307.2 million and principal payment is Rs. 5690.6 million. In fiscal year 2007/08 the government expenditure is Rs. 161350.02 million, which includes recurrent expenditure Rs. 91446.99 million, capital expenditure Rs. 53516.10 million and principal payment Rs. 16386.93 million. The following table shows the government expenditure in different fiscal year.

**Table No. 4.9**  
**Government expenditure**

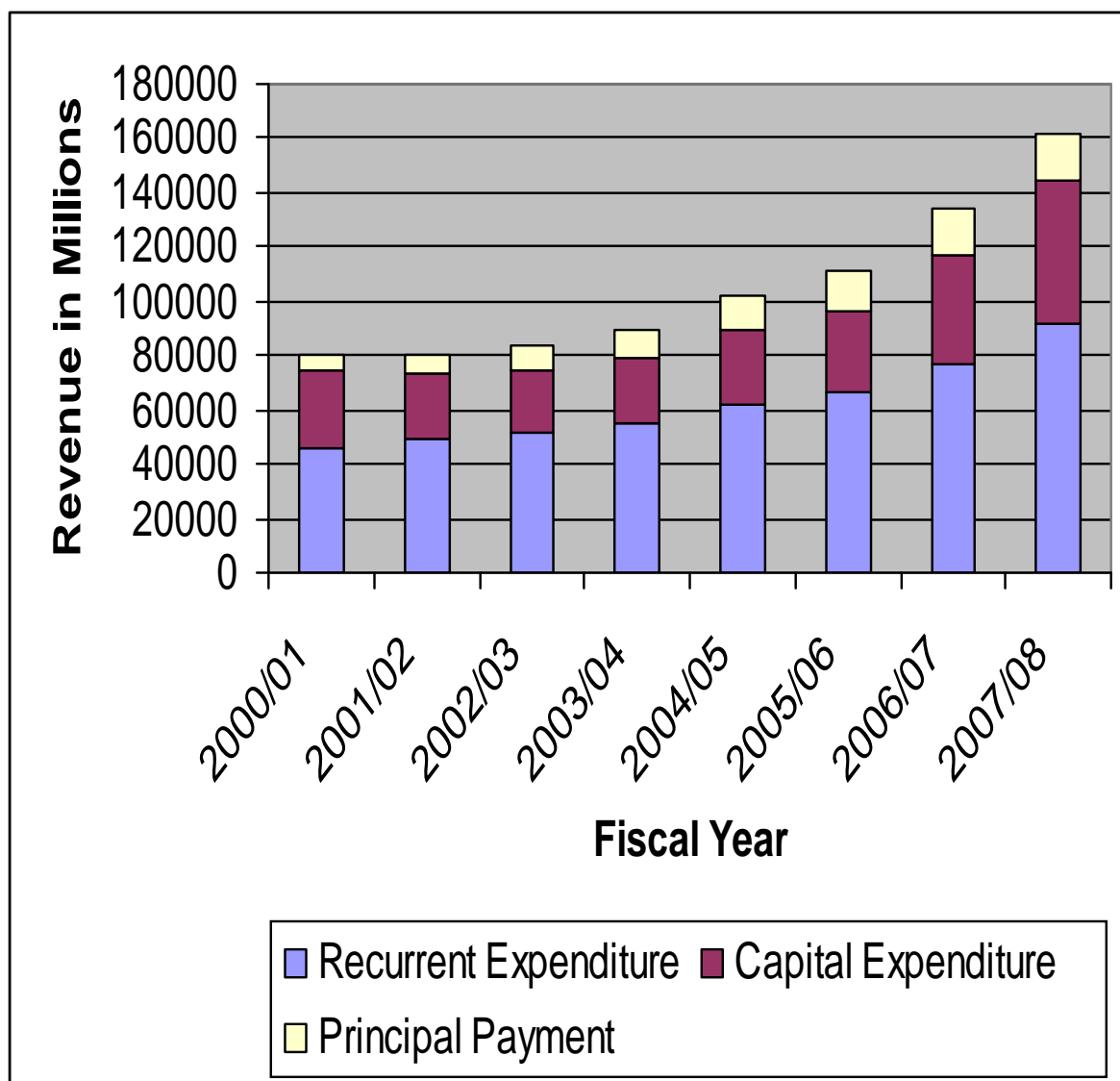
**Rs. in Million**

Fiscal year	Government expenditure			Total
	Recurrent expenditure	Capital expenditure	Principal expenditure	
2000/01	45837.3	28307.2	5690.6	79835.10
2001/02	48863.9	24773.4	6434.9	80072.20
2002/03	52090.5	22356.1	9559.5	84006.10
2003/04	55552.1	23095.6	10794.9	89442.60
2004/05	61686.4	27340.7	13533.3	102560.40
2005/06	67017.8	29606.6	14264.8	110889.20
2006/07	77122.40	39729.90	16752.50	133604.60
2007/08	91446.99	53516.10	16386.93	161350.02

Source: Economic Survey 2008/09, MOF.

The above explanation can be shown in following figure.

**Figure No. 4.9**  
**Government Expenditure**



#### 4.1.10 Government Receipts

Government receipts include the total tax and non tax revenue and foreign grants. The main source of government receipts is revenue. Total government receipts in fiscal year 2000/01 was Rs. 55647.0 million which includes Rs. 48893.6 million from revenue and Rs. 6753.4 million from grants. Similarly total government receipts in different fiscal year and its composition is given in following tables.



**Table No. 4.10**  
**Government Receipts**

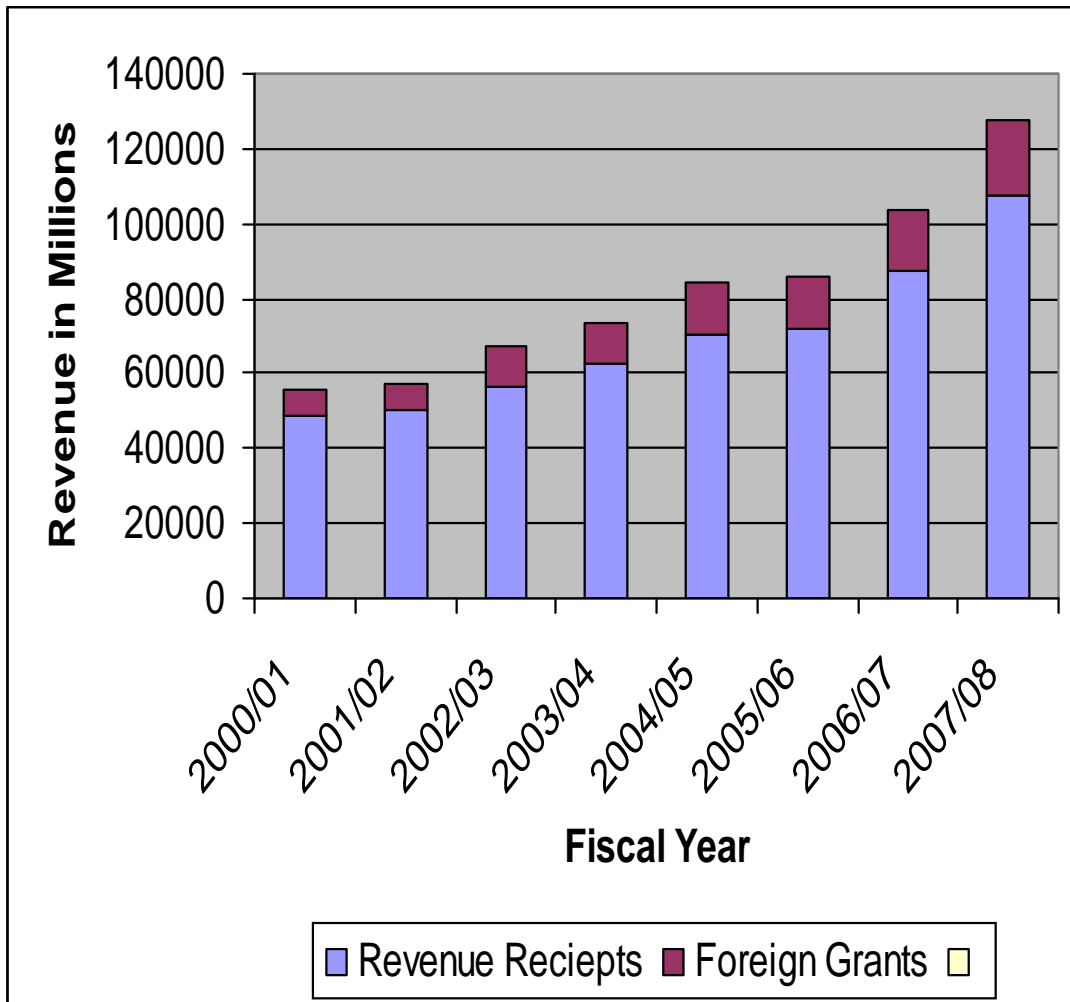
Rs. in million

Fiscal Year	Revenue receipts	Foreign grants	Total receipts
2000/01	48893.6	6753.4	55647.0
2001/02	50445.5	6686.1	57131.60
2002/03	56229.8	11339.1	67568.9
2003/04	62331.0	11283.4	73614.4
2004/05	70122.7	14391.2	84513.9
2005/06	72282.1	13827.5	86109.6
2006/07	87712.10	15800.80	103512.90
2007/08	107622.58	20320.73	127943.31

Source: Economic Survey 2008/09, MOF.

Government receipts from revenue and foreign grants in different year can be shown in figure. Following figure shows the total receipts from revenue and foreign grants in different fiscal year.

**Figure No. 4.10**  
**Government receipts composition**



**4.1.11 Comparative study of government receipts and expenditure**

Government collects revenue from different sources; they are tax revenue, non tax revenue and foreign grants. Government expenditure head mainly are recurrent expenditure, capital expenditure and principal repayment. Government collects revenue and grants and expenses in different heads. If receipt is more than expenditure there is surplus, if expense is more than revenue there is deficit. Following table shows the government receipts, expenditure and surplus & deficit relation.

**Table No. 4.11****Comparative Study of government receipts and expenditure**

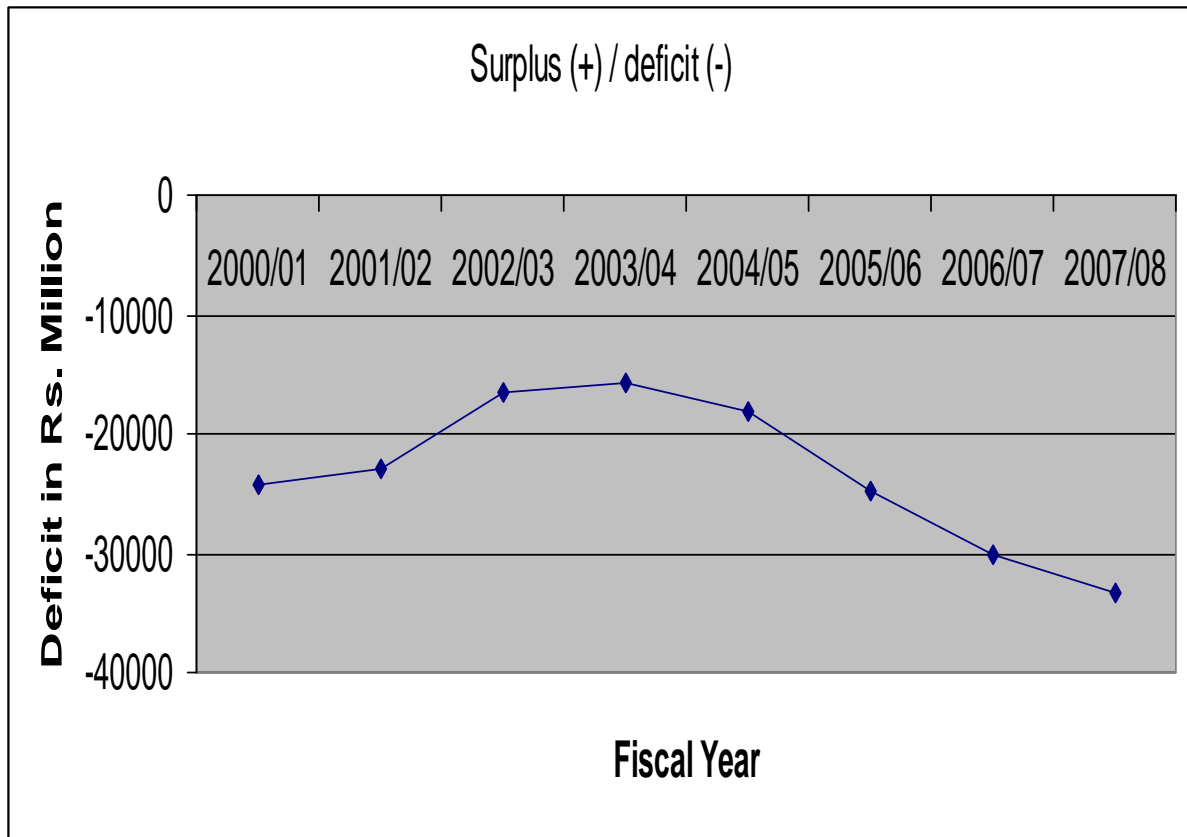
Rs. in million

Fiscal Year	Expenditure	Receipts	Surplus (+) / deficit (-)
2000/01	79835.1	55647.0	-24188.10
2001/02	80072.2	57131.6	-22940.60
2002/03	74006.1	67568.9	-16437.2
2003/04	89442.6	73614.4	-15828.2
2004/05	102560.4	84513.9	-18046.50
2005/06	110889.2	86109.6	-24779.60
2006/07	133604.6	103512.90	-30091.70
2007/08	161350.02	127943.31	-33406.71

Source: Economic Survey 2008/09, MOF.

The above table shows the relation between government expenditure and government revenue. The table clearly shows the government expenditure is more than government receipts in and every year. In every year, there is deficit because expenditure is more than receipts. The deficit in fiscal year 2000/01, FY 2001/02, FY 2002/03, FY 2003/04, FY 2004/05, FY 2005/06 , FY 2006/07 and FY 2007/08 was Rs. 24188.1 million, Rs. 22940.6 million, Rs. 16437.2 million, Rs. 15828.2 million, Rs. 18046.5 million, Rs. 24779.6 million , Rs. 30091.7 million and 33406.71 million respectively. The above explanation can be shown in following figure also.

**Figure no. 4.11**  
**Trend of deficit**



#### 4.1.12 Exemption Limit in Nepal

Exemption limit directly influences revenue collection from income tax. Taxpayer having low tax paying capacity should exclude from the tax net for the social justice and economic balance between rich and poor. The exemption limit provided in the various years is presented in the table 4.12. In the earlier time, there was equal amount of exemption to all the taxpayers i.e. individual, couple, family and corporate bodies. Exemption limit to all taxpayers was Rs. 7000 in the FY 1959/60 to FY 1962/63. The exemption limit to the corporate taxpayer was curtailed from the FY 1965/66. The exemption limit to the couple and family was equal each year except FY 1967/68 to FY 1973/74 and FY 1975/76 to FY 1978/79. The exemption limit to the family was Rs. 6000 in the FY 1967/68 to FY 1973/74 whereas it was Rs. 4500 to the couple. The exemption limit to couple and family was Rs. 6500 and 7500 respectively in the FY 1974/75 and it was further extended by Rs. 1000/1000 for the fiscal year 1976/77 to 1978/79.

From the table, it is clear that exemption limit is extended according to need of time and income condition. At present time, individual having taxable income up to Rs. 115000 are exempted from tax and that for couple is Rs. 140000.

Note that if it is pension income of a resident person, the exemption limit would be exemption amount plus 25 percent of exemption amount. A disable resident individual is entitled to a 50% basic exemption as additional exemption.

**Table No. 4.12**  
**Exemption Limit in Nepal**  
**From Fiscal year 1959/60 - 2005/06**

<b>Fiscal Year</b>	<b>Individual</b>	<b>Couple</b>	<b>All taxpayers</b>
1959/60-1962/63	-	-	7000
1963/64-1964/65	-	-	6000
1965-66-1966/67	-	-	5000
1967/68-1973/74	3000	4500	-
1974/75	4500	6000	-
1975/76	5500	6500	-
1976/77-1978/79	6500	7500	-
1979/80-1980/81	7500	10000	-
1981/82-1982/83	10000	15000	-
1983/84-1989/90	15000	20000	-
1990/91-1991/92	20000	30000	-
1992/93-1996/97	25000	35000	-
1997/98	30000	40000	-
1998/99	40000	50000	-

1999/00	55000	75000	-
2000/01	55000	75000	-
2001/02	65000	85000	-
2002/03	65000	85000	-
2003/04	80000	100000	-
2004/05	80000	100000	-
2005/06	100000	125000	-
2006/ up to now	125000	140000	-

Source: Finance Acts of Various year, Ministry of Finance

## **4.2 Analysis of Primary data**

### **4.2.1 Introduction**

The survey result has been done to ascertain the various aspects of income tax in Nepal. The structured questionnaire was prepared and distributed to the respondents for this purpose. The opinion of the various 75 respondents associated with distinct denominations i.e. tax administration, tax expert and tax payers were collected. The questionnaire has covered role of income tax, major problem of income tax system, problems faced by tax payer, the most important factors for the effectiveness of income tax system in Nepal (see the format of questionnaire in an appendix 1). The respondents were asked either to response yes/no or for ranking of choices according to number of alternatives where first choice was the most important and last choice was least important. Number of respondents in each denomination is equal 25. Information received from the respondents are tabulated and analyzed in the proper way.

**Table No. 4.13**  
**Group of Respondents and Number from each Group**

S.N.	Group of Respondents	No.
1.	Group tax administrators	25
2.	Income tax experts	25
3.	Income tax payers	25
	<b>Total</b>	75

Source: Estimated figure

#### 4.2.2 Result of Empirical Investigation

##### 4.2.2.1 Income tax as suitable means of raising government revenue:

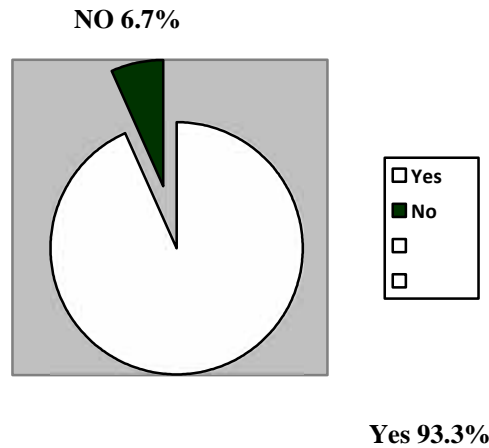
To know whether income tax as a suitable means of raising government revenue in Nepal, a question was asked "Do you consider that income tax is suitable means of raising government revenue in Nepal?" The respondent's responses are tabulated in the following table.

**Table No. 4.14**  
**Income tax as a suitable means of raising revenue**

Response Respondents	Yes		No		Total	
	No	Percentage	No	Percentage	No.	Percentage
Tax Administrator	23	92	2	8	25	100
Tax Expert	24	96	1	4	25	100
Tax payers	23	92	2	8	25	100
Total	70	93.3	5	6.7	75	100

Source: Field Survey 2010.

**Figure No. 4.12**  
**Income tax as a suitable means of raising revenue**



From the opinion survey, it is found that 92 percent of tax administrators 96% of tax experts and 92 percent of Tax payers recognize Income Tax as a suitable means of raising government revenue. Only 8 percent tax administrators and 4% of tax expert and 8 percent of tax payers does not recognize. In aggregate, 93.3 percent respondent recognized and 6.7 percent does not recognized income tax as a suitable means of raising government revenue in Nepal. Thus, it can be said that income tax is a suitable means of raising government revenue in Nepal.

**4.2.2.2 Need of Public awareness program**

To know the respondents opinions towards public awareness program the question was put "Do you think that public awareness program is necessary in Nepal for raising the government revenue?" to them. The opinion result has been summarized in the following table.



**Table No. 4.15****Need of Public awareness program**

<b>Response Respondents</b>	<b>Yes</b>		<b>No</b>		<b>Total</b>	
	<b>No</b>	<b>Percentage</b>	<b>No</b>	<b>Percentage</b>	<b>No.</b>	<b>Percentage</b>
Tax Administrator	24	96	1	4	25	100
Tax Expert	23	92	2	8	25	100
Taxpayer	25	100	-	-	25	100
Total	75	96	-	4	75	100

Source: Field Survey 2010.

From the above opinion survey that 96% of tax administrators, 92% of tax experts and 100% of tax payers approved that public awareness program are necessary in Nepal for raising government revenue. In average 96% of respondents have approved. Only 4% of them have not approved. Thus, it can be concluded that public awareness program is very much necessary for raising Nepalese government revenue.

#### ***4.2.2.3 Contribution of Income Tax Revenue***

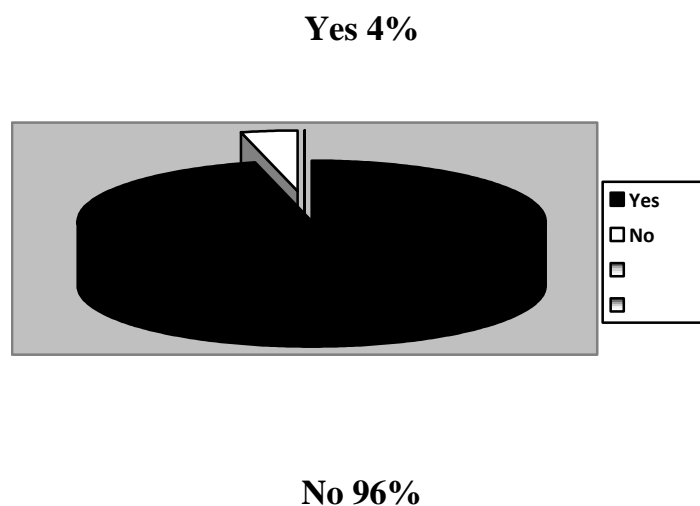
Income tax has contributed about 20 percent of total revenue in Nepal. It is criticized that contribution of income tax to national is not satisfactory. To know the real fact, the question was asked to respondent "In your opinion, is contribution of income tax to total revenue of Nepal satisfactory?" Opinion result has been presented in the following table.

**Table No. 4.16**  
**Satisfactory Contribution of Income Tax Revenue**

Response Respondents	Yes		No		Total	
	No	Percentage	No	Percentage	No.	Percentage
Tax Administrator	1	4	24	96	25	100
Tax Expert	2	8	23	92	25	100
Taxpayer	-	-	25	100	25	100
Total	3	4	72	96	75	100

Source: Field Survey 2010.

**Figure No. 4.13**  
**Satisfactory Contribution of Income Tax Revenue**



Only 4 percent of tax administrators and 8 percent of taxpayers approve that income tax contribution to public revenue is satisfactory. But 100 percent tax payers argue that contribution of income tax to total revenue in Nepal is unsatisfactory. In

aggregate, 4% percent respondents argue that Nepalese income tax contribution is satisfactory.

#### 4.2.2.4 Reasons for low contribution of Income Tax

In order to find out those major reasons for lower contribution of income tax, next question was asked, "If no, what are the major reasons." The respondents were requested to rank their choice from 1 to 5 according to preference.

**Table No. 4.17**  
**Reasons for Low contribution of Income Tax to Total Revenue**

S.N.	Method	Total Points Received				Percentage	Rank
		Tax Administrator	Tax Expert	Tax Payer	Total		
1.	Defective of Income Tax Act	80	73	99	252	24	4
2.	Mass poverty and low income level	53	80	49	182	17.33	2
3.	Increasing habit of tax evasion	55	34	77	166	15.80	1
4.	Inefficient income tax administrator	89	52	42	183	17.43	3
5.	Inappropriate rate and exemption limit	68	91	108	267	25.44	5
	Total				1050	100	

Source: Field Survey 2010

In table rank 1 is given to the lowest percentage and 5 to the highest. Here lowest percentage is obtained by the method which is regarded highly appropriate by the respondents. In the questionnaire, the respondents were requested to given number 1 to the most appropriate of last to the last appropriate.

From the above table, the major reasons for low contribution of income tax to total revenue ranked in order of preference of the respondents are as follows:

1. Increasing habit of tax evasion.
2. Mass poverty and low income level
3. Inefficient income tax administration
4. Defective income tax act
5. Inappropriate rate and exemption limit

#### ***4.2.2. 5 Contribution of Direct Tax***

Direct tax includes tax on poverty, tax on income, tax in interest and other taxes. The contribution of direct tax to total revenue is about 21 percent in average.

To know whether the contribution of direct tax to national revenue is effective or not, a question was asked, "Do you think that contribution of direct tax to total revenue is effective?" The responses are tabulated in following table.

**Table No. 4.18**

**View towards Effective Contribution of Direct Tax**

Response Respondents	Yes		No		Total	
	No	Percentage	No	Percentage	No.	Percentage
Tax Administrator	5	20	20	80	25	100
Tax Expert	10	40	15	60	25	100
Taxpayer	8	32	17	68	25	100
Total	26	30.6	49	69.4	75	100

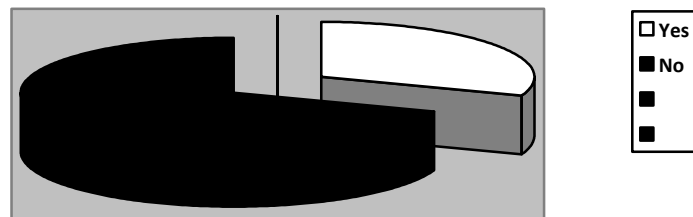
Source: Field Survey 2010.

**Figure No. 4.14**

**Views towards Effective Contribution of Direct Tax**

**Yes 30.6%**

**No 69.4%**



Only 20 percent of tax administrator 40 percent of tax expert and 32 percent of taxpayer recognized the contribution of direct tax to total revenue is effective. 69.4

percent respondent did not approve that contribution of direct tax to total revenue is effective. From this opinion, it can be concluded that the contribution of direct tax to total revenue is not effective.

#### **4.2.2. 6 Appropriateness of Exemption and Deduction**

Adequate exemption and deduction is necessary to promote the business enterprises. Many exemption and deduction are provided by "Industrial Enterprises Act, 2049" and "Income Tax Act, 2058". The question "Are exemption and deduction provided by Act appropriate?" was asked to know the opinion of the respondents regarding the exemption and deduction. Opinion result has been summarized in the table given below.

**Table No. 4.19**  
**Appropriateness of Exemption and Deduction**

<b>Response Respondents</b>	<b>Yes</b>		<b>No</b>		<b>Total</b>	
	<b>No</b>	<b>Percentage</b>	<b>No</b>	<b>Percentage</b>	<b>No.</b>	<b>Percentage</b>
Tax Administrator	2	8	23	92	25	100
Tax Expert	5	20	20	80	25	100
Taxpayer	1	4	24	96	25	100
<b>Total</b>	<b>8</b>	<b>10.6</b>	<b>67</b>	<b>89.4</b>	<b>75</b>	<b>100</b>

Source: Field Survey 2010

Only 10.6 percent of respondent agree with present exemption and deduction. But large figure i.e. 89.4 percent respondents disagree with the present exemption and deduction.

#### 4.2.2.7 *Appropriate Method of Income Tax Assessment*

Contribution of income tax to total revenue also depends on the income tax assessment procedures. Therefore, assessment procedure should be appropriate and effective. A question, "Which income tax assessment method is more appropriate in Nepal?" was asked to know the respondents' opinion about appropriate method of income tax assessment. The responses have been presented in the table below:

**Table No. 4.20**  
**Appropriate Method of Income Tax Assessment**

<b>S.N.</b>	<b>Methods</b>	<b>Tax Administrator</b>	<b>Tax Expert</b>	<b>Tax Payer</b>	<b>Total</b>	<b>Percent</b>
1	Self Assessment	15	23	25	63	84
2	Jeopardy Assessment	-	2	-	2	2.6
3	Amended Assessment	8	-	-	7	10.66
	Total	25	25	25	75	

Source: Field Survey 2010

84 percent respondents approved self-tax assessment method is more appropriate to assess income tax. 2.6 percent respondents are in favor of jeopardy assessment and 10.66 percent in favor of amended assessment. The respondent category that is most in favors of self-assessment is taxpayers. From the above opinion, it can be concluded that self-tax assessment method is more appropriate while assessing income tax to collect large amount of revenue through income tax. But during the survey, the opinion of one of the respondent was that, there are not mutually related. So they all are equally important.

#### 4.2.2. 8 Attitude toward problems in paying Income Tax

To know the problems facing by the taxpayers while paying income tax, the respondents were requested to rank their choice from 1 to 5 according to their preference. The question was, "In your thinking, what types of problems are facing by the tax payer while paying income tax." Responses received from respondents are tabulated in the table.

**Table No. 4.21**  
**Problems in Tax Paying**

S.N.	Problems	Points Received				Percent	Rank
		Tax Administrator	Tax Expert	Tax Payer	Total		
1	Consuming unnecessary time	66	82	133	281	24.98	5
2	Exception of illegal incentives by tax personnel	90	71	61	222	19.73	2
3	Vague provision in income tax laws	48	47	51	146	12.98	1
4	Lengthy process	70	88	94	252	22.50	4



5	Lack of cooperation by tax administrator	111	57	56	224	19.90	3
	Total				1125	100.00	

Source: Field Survey 2010.

In table no. 4.16 Rank 1 is given to the lowest percentage and 5 to the highest. Here lowest percentage is obtained by the problem which is treated as the important problem by the respondents. In the questionnaire, the respondents were requested to given number 1 to the most appropriate of last to the least appropriate.

From the table, the major problems facing by the taxpayer while paying income tax ranked in order of preference of the respondents are as follows:

1. Vague provision in income tax laws.
2. Expectations illegal incentives to the personnel
3. Lack of Co-operation by tax administrator
4. Lengthy process
5. Consuming unnecessary time

#### **4.2.2. 9 Reasonableness of Existing Provision of Fines and Penalty**

Fines and Penalty also play significant role to reduce the tax evasion and illegal activities and make morality to the tax payer. To know the views of respondents about the find and penalty, the respondents were requested to tick yes/no option. The question was, "Are the provisions of fines and penalty under the Nepalese tax system reasonable?" The opinion of respondents tabulated in the table.

**Table No. 4.22****Reasonableness of existing provision of Fines and Penalty**

<b>Response Respondents</b>	<b>Yes</b>		<b>No</b>		<b>Total</b>	
	<b>No</b>	<b>Percentage</b>	<b>No</b>	<b>Percentage</b>	<b>No.</b>	<b>Percentage</b>
Tax Administrator	15	60	10	40	25	100
Tax Expert	16	64	9	36	25	100
Taxpayer	2	8	23	92	25	100
<b>Total</b>	<b>33</b>	<b>44</b>	<b>42</b>	<b>56</b>	<b>75</b>	<b>100</b>

Source: Field Survey 2010.

44 percent respondents are in favor of present provisions of fines and penalty but 56 percent respondent is against the present provisions of fines and penalty. Out of totals taxpayer respondent, the highest 92 percent are against the present fine and penalty.

In order to know reasons of unreasonable fine and penalty provisions, the next question was asked, "If no, how should it be made reasonable?" Views of respondents are tabulated in the table.

**Table No. 4.23****Reasonable Fine and Penalty Rate**

<b>Respondents</b>	<b>By Increasing</b>		<b>By Decreasing</b>		<b>Total</b>	
Tax Administrator	10	100	-	-	10	100
Tax Expert	9	100	-	-	9	100
Tax Payer	2	8.7	21	91.3	23	100
<b>Total</b>	<b>21</b>	<b>69.6</b>	<b>21</b>	<b>30.7</b>	<b>42</b>	<b>100</b>

Source: Field Survey 2010.

69.6 percent of the respondents, who were against percent fines and penalty, gave their views for increasing fine and penalty and 30.7 percent gave view in the favor of decreasing rate. The unsatisfied tax administrators and tax experts are totally in favors if increasing fines and penalty.

#### **4.2.2. 10 Soundness of Income Tax System in Nepal**

To know the respondents view regarding soundness and efficient of income tax system in Nepal, a question, "In your opinion is income tax system of Nepal sound and efficient"? Was asked the responses are tabulated in the table.

**Table No. 4.24**  
**Soundness of Income Tax System in Nepal**

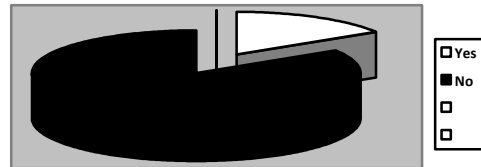
<b>Response Respondents</b>	<b>Yes</b>		<b>No</b>		<b>Total</b>	
	<b>No</b>	<b>Percentage</b>	<b>No</b>	<b>Percentage</b>	<b>No.</b>	<b>Percentage</b>
Tax Administrator	10	40	15	60	25	100
Tax Expert	2	8	23	92	25	100
Taxpayer	-	-	25	100	25	100
<b>Total</b>	<b>12</b>	<b>16</b>	<b>63</b>	<b>84</b>	<b>75</b>	<b>100</b>

Source: Field Survey 2010.

**Figure No. 4.15**

**View towards income tax system in Nepal**

Yes 16%



No 84%

84 percent respondent approve that income tax system of Nepal is not sound and efficient. Only 16 percent respondents approved soundness and efficient tax system of Nepal.

**4.2.2. 11 Effectiveness of Income Tax Administration**

To know the respondents view regarding effectiveness of income tax administration in Nepal a question, "Do you agree that Nepalese income tax administration is effective?" was asked. The responses are tabulated in the following table.

**Table No. 4.25**  
**Effectiveness of Income Tax administration in Nepal**

Response Respondents	Yes		No		Total	
	No	Percentage	No	Percentage	No.	Percentage
Tax Administrator	15	60	10	40	25	100
Tax Expert	4	16	21	84	25	100
Taxpayer	1	4	24	96	25	100
Total	20	26.6	55	73.3	75	100

Source: Field Survey 2010.

From the table it has been clear that Nepalese income tax administration is not effective. Most of the respondents i.e. 73.3 percent of respondents recognize it ineffective. The high percentage of respondent who are in favors of Nepalese tax administration is the tax administrators themselves.

#### ***4.2.2. 12 Suitable Tax Rate in Nepal***

In order to find out the suitable income tax rate system in Nepal, respondents were requested to select any among the three alternatives. The question was "In your opinion, which income tax rate is suitable for Nepal?" The responses are tabulated in the table.

**Table No. 4.26**  
**Appropriate Method of Income Tax Assessment**

<b>S.N.</b>	<b>Methods</b>	<b>Tax Administrator</b>	<b>Tax Expert</b>	<b>Tax Payer</b>	<b>Total</b>	<b>Percent</b>
1	Progressive	23	25	15	63	84
2	Proportional	2	-	10	12	16
3	Regressive	-	-	-	-	-
	Total	25	25	25	75	

Source: Field Survey 2010.

From the table it is clear that, 84 percent of respondents prefer progressive income tax rate in Nepal. So, it can be concluded that progressive tax rate is most suitable means of tax rate in Nepal.

#### **4.2.2. 13 Most important factors for effectiveness of Income Tax**

The respondents were requested to rank their choice from 1 to 5 according to their preference to know the opinion of the respondents' view regarding to important factors for effectiveness of income tax in Nepal. A question, "In your opinion, what is the most important factor for effectiveness of income tax in Nepal to raise government revenue?" was asked. Responses are summarized in table.

**Table No. 4.27****Most important factors for effectiveness of Income Tax**

S.N.	Factors	Points Received				Percent	Rank
		Tax Administrator	Tax Expert	Tax Payer	Total		
1	Clear Act, Rules and Regulations	79	70	90	239	21.24	4
2	Conscious and honest tax payers	31	65	55	151	13.42	1
3	Moral and honest tax officers	60	75	45	180	16.00	2
4	Effective tax administration	98	60	70	228	20.27	3
5	Political non interruption	107	105	115	327	29.10	5
	Total				1125	100.00	

Source: Field Survey 2010.

In table rank 1 is given to the lowest percentage and 5 to the highest. Here lowest percentage is obtained by the factor which is regarded highly appropriate by the respondents. In the questionnaire, the respondents were requested to give number 1 to the most appropriate of last to the least appropriate.

The important factors for effectiveness of income tax in Nepal according to the preference of the respondents were as follows:

1. Conscious and honest tax payers
2. Moral and honest tax officers
3. Effective tax administration
4. Clear act, rules and regulation
5. Political non interruption

### **4.3 Major findings of the study**

After analyzing the data from primary and secondary sources we get some important findings about contribution of income tax in total revenue of Nepal are as follows.

#### **4.3.1 Findings from the secondary data**

- ) Government expenditure is in increasing trend. In fiscal year 2000/01 total expenditure of government was Rs. 79835.1 million, in FY 2001/02 the total expenditure Rs. 80072.2 million similarly in fiscal year 2006/07 the total government expenditure was Rs. 133604.60 million. and in FY 2007/08 total government expenditure was Rs. 16350.02 million. It shows the government expenditure is increasing each and every year.
- ) Government expenditure includes recurrent expenditure, capital expenditure and principal payment. And government receipts include revenue and foreign grants. If government expenditure is equal to government receipt that is balance budget. If receipt is more than expenditure that is surplus budget. And if receipt is less than expenditure that is deficit budget. In Nepal, each and every year's expenditure is more than revenue. That is deficit budget.
- ) Government receipt includes revenue and foreign grants. The main source of receipt is revenue which is more than 80% in total receipts.



- ) Total receipts in fiscal year 2000/01 was Rs. 55647.0 million similarly in fiscal year 2001/02, 2002/03, 2003/04, 2004/05 , 2006/07 and 2007/08 was Rs. 57131.6 million, Rs. 67568.9 million, Rs. 73614.4 million, Rs. 84513.9 million, Rs. 86109.6 million, Rs. 103512.90 million and 127943.31 respectively.
- ) In Nepal the government expenditure is more than government revenue so there is deficit budget the deficit amount of different fiscal year 2000/01 was Rs. 24188.1 million and n 2001/02 Rs. 22940.6 million, in fiscal year 2002/03 was Rs. 16437.2 million in fiscal year 2003/04 was Rs. 15828.2 million similarly in fiscal year 2004/05 FY 2005/06 ,FY 2006/07 and FY 2007/08 was Rs. 18046.5 million, Rs. 24779.6 million , Rs. 30091.70 and 33406.71 million respectively.
- ) The deficit budget does not play important role in the economy so the government should increase the receipts. To increase the total receipts the government should collect more revenue from tax because foreign grants is not good way to raise the revenue.
- ) Nepalese government revenue is the composition of direct tax revenue and indirect tax revenue the direct tax revenue is in decreasing trend the indirect tax revenue play the dominant role in the economy.
- ) The main sources of tax revenue is tax from customs, tax on consumption and product of goods and services, land revenue and registration and tax on property, profit and income.
- ) Total tax collection in FY 2000/01 Rs. 38865.1 million, in FY 2001/02 Rs. 393306.6 million in FY 2002/03 Rs. 42587.8 million, in FY 2003/04 Rs. 48173.0 million, similarly in FY 2004/05, FY 2005/06 , FY 2006/07 and FY2007/08 was Rs. 54104.7 million, Rs. 57430.4 million and 71126.7 million and 85155.54 respectively.
- ) Tax collection from customs includes tax from imports, exports, Indian excise duty and others. Tax collection from customs in fiscal year 2000/01 was Rs. 12552.1 million, similarly in FY 2001/02, FY 2002/03, FY 2003/04, FY 2004/05, FY 2005/06, FY 2006/07and FY 2007/08 were 12658.8 million,

Rs. 14236.4 million, Rs. 15554.8 million, Rs. 15701.6 million, Rs. 15344.0 million and Rs. 16707.6 million and Rs. 21062.5 respectively.

- J Tax collections from consumption product of goods and services in FY 2000/01 to FY 2007/08 were Rs. 16153.6 million, Rs. 16074.3 million, Rs. 18244.8 million, Rs. 20705.6 million, Rs. 255331.8 million, Rs. 28118.3 million and Rs. 35438.8 million and Rs. 41005.32 millions respectively. This shows the revenue collection from consumption product is higher than other tax sources.
- J Income tax collection from property, profit and income in FY 2000/01 was Rs. 9546.5 million in FY 2001/02 was Rs. 946.7 million in FY 2002/03, Rs. 8691.5 million similarly in FY 2003/04, FY 2004/05, FY 2005/06, FY 2006/07 and 2007/08 were Rs. 10215.1 million, Rs. 11272.6 million and Rs. 16726.8 million and Rs. 20147.02 respectively.
- J The contribution of income tax in total revenue of Nepal in FY 2000/01 was 23.45%, in FY 2001/02 was 22.64%, in FY 2002/03 was 18.71%, in FY 2003/04 was 19.19%, in FY 2004/05 was 18.78%, in FY 2005/06 was 18.06% and in FY 2006/07 was 21.14% and 20.33 respectively
- J Income tax exemption limit in Nepal was Rs. 7000 for all taxpayer in FY 1959/60 but at present income tax exemption tax exemption limit is Rs. 115000 for individuals and Rs. 140000 for couples and family in FY 2008/09. The exemption limit is not provided for partnership firms, corporation and non-residents. It is found that exemption limit has been changed according to time and income.
- J Increment in the number of taxpayers is very much essential in order to broaden the tax base. Number of registered income taxpayers in Nepal for the FY has increased in comparison to previous year.

#### **4.3.2 Findings from the study of primary data**

An opinion survey has been conducted in order to find out the role of income tax in Nepal and some other aspects of income tax. From the opinion survey with tax administrators, tax experts and taxpayers, the following findings have been drawn.

- a. Income tax is the suitable means of raising government revenue.
- b. Public awareness program is necessary to increase tax consciousness and raising the government revenue.
- c. Mass poverty and low income level, increasing habit tax evasion, inefficient income tax administrations etc are the major reasons for the Low contribution of income tax to national revenue.
- d. Contribution of direct tax to total revenue is not effective.
- e. Exemption and deduction should be increased to promote the special industry and export.
- f. To increase the voluntary compliance by taxpayer, self-assessment method is the appropriate method while assessing the income tax.
- g. Lengthy process, vague provision in income tax laws, consuming unnecessary time etc are the major problems facing by the taxpayer while paying the tax.
- h. The fines and penalty under the Nepalese tax system are not reasonable and it should be increase to discourage tax evader and illegal activities.
- I. Income tax system of Nepal has not reached at the satisfactory level yet.
- J. Income tax system of Nepal has not reached at the satisfactory level yet.
- k. The current income tax administration is not running satisfactorily and is not efficient.
- l. Progressive income tax rate is considered as the suitable means of tax in Nepal.
- m. Clear act, rules and regulation, effective tax administration are the most important instruments for effectiveness of income taxation in Nepal.

# Chapter 5

## SUMMARY, CONCLUSION AND RECOMMENDATION

### 5.1 Summary

A government requires sufficient fund to lunch the development programs to handle the daily administration to keep peace and security and to lunch other public welfare programs. For that government collects funds from various sources such as, taxes, fees, special assessment, fine and penalties, foreign grants etc. Funds are generally called revenue in the language of government. Among various sources of revenue, tax is the main source of collecting the public revenues because it occupies the most important part of the government treasure.

Tax is compulsory payment made to the government by a person from his/her taxable income according to law. Tax is contributed to the government without expectation of any direct benefit. In the broad sense there are two types of taxes: direct and indirect tax. Income tax, gift tax, interest tax, property tax, vehicle tax, house & land tax, contract tax etc are the example of direct tax. Export/import duty, excise duty, sales tax, value added tax, entertainment tax, hotel tax, passenger tax are example of indirect tax.

The idea of introducing income tax in Nepal originated along with the first budget on 21Magh 2008 (1952). Then the first elected government introduced "Business profit and remuneration Act 2017" to impose income tax on remuneration and business profit in Nepal. Business profit and remuneration tax act 2017 had so narrow coverage that income tax was imposed only on business profit and remuneration. It was replaced by the Nepal income tax act 2019 after two years. After that income tax rule 2020 were enacted with the view of implementations the objective of the income tax act. As "Nepal income tax act 2019" was incapable to fulfill the needs of the time, it was replaced by another income tax act 2031. In the course of development and modernization of income tax system the new income tax act 2058 has been enacted. Similarly the new income tax rules 2059 have also been enacted for the

effective implementation of the objective of the act. Income tax act 2058 has classified the heads of income in to three categories viz. employment, business and investment.

Now, individual income tax is levied with two rates 15% and 25% while corporate income tax is levied with a single or flat rate of 25% however bank and financial institutions are liable to pay income tax @ 30% of taxable income. The special industrial enterprises are liable to pay income tax only at the rate of 20% of taxable income. The industry established in backward and operated in remove area are entitled some facilities concessions and rebates.

When a person derives an amount or incurs expenses, tax is determined according to Generally Accepted Accounting Principle (GAAP) considering the provisions made by the act. As per the law natural person is required to maintain the accounts on the cash basis. A company is required to maintain the accounts on the accrual basis within the framework of GAAP. Other entity operating a business or having investment may adopt either cash or accrual basis for maintaining its accounts. Similarly a natural person operating a business may adopt either cash or accrual basis unless the department prescribes by written notice.

Income tax act 2058 intends to bring all the incomes in to the area of tax. However certain incomes of some individuals or entities are especially exempt from income tax by the law. Further more the act has provided the facilities of relaxing with the concession tax rate for specified individuals or entities.

Income tax is imposed on taxable income that is obtained by subtracting deductible expenses from chargeable incomes. But sometimes a taxpayer may face the situation of loss due to the occurrence of deductible expenses in excess of chargeable incomes. In respect of business or investment a taxpayer is entitled to set off or carry backward on forward of such unrelieved loss as per tax law. The unrelieved loss of an income year incurred by a person from any business or investment is calculated as calculated as the excess of deductible expenses over chargeable income ignoring the treatment of unrelieved losses.

Income tax assessment refers to the procedure of ascertaining the taxable

income and tax liability of a person and tax payable by a person. Income tax is assessed adopting different methods of tax assessment practiced in Nepal are self assessment, jeopardy assessment and amended assessment.

To fulfill the general objective of this study different source of data are used to find out the accurate and actual conclusion. Mainly the secondary data are collected from economic survey, published by ministry of finance Nepal government annual report published by Inland Revenue department and other publicities. And primary data are used from field survey in different area of Janakpur municipality.

. By analyzing the secondary data it is found that government expenditure is in increasing trends every year .On the other hand government receipts are also increasing. But the expenditure is more than the receipts in every year. So there is deficit budget in every year .The sources of government receipts are : government revenue and foreign grants. Foreign grants are not better sources of receipts. It is not sure in every year so the government revenue is better sources of government receipts. The government collects revenue from tax and non tax revenue. Tax revenue includes tax from customs , tax on consumption and product of goods & services, land revenue and registration, tax on property , profit and income. Among them the main source of receipts of government revenue is customs and tax on consumption and product and services.

Total tax revenue collection in fiscal year 2007/08 was Rs. 85155.54 million and non tax revenue Rs. 22467.04 million. According to the field survey, most of the respondents are conscious about the payment of tax. But they have no proper knowledge about it. The government should conduct the awareness programs about it.

## **5.2 Conclusion**

The government need huge amount of revenue to achieve the objectives of nation. In developing countries like Nepal, lack of sufficient financial resource is the main constraint for the economic development. Nepal is facing serious problem of resource

gap and high dependency on foreign loan. Resource gap is increasing at a faster rate than the increase in revenue. The resource gap is widening continuously with the increment of total expenditure in respect to total revenue collection. To solve such serious problem of financial deficit, income tax should play important role. But, resource mobilization in Nepal is still poor. Developing country like Nepal utilize external borrowing as a technique to address the gap between the government revenue and investment as well as to meet the export-import gap. This kind of borrowing adds to the total resources available to the government over a given period and enables the government to incur higher expenditure than would be otherwise possible. These resources can contribute to poverty alleviation and economic growth if properly employed .

The government of Nepal introduced a formal tax for the first time in Nepal in 1959 (2017 B.S.) in the form of "Business profits and Remuneration Tax." According to this Act, incomes only from Business profits and remuneration were subjected to tax. At present, in Income Tax Act, 2002 which became effective since April 1<sup>st</sup> 2002, sources of Nepalese income are classified into Business income, investment income and employment income for the tax purpose. The percentage share of income tax to government revenue is not satisfactory in comparison to other developing countries like India, Pakistan, Bangladesh and Sri Lanka etc. There are three major income tax assessment methods in Nepal. Currently, income tax revenue in Nepal is collected through four sector i.e. corporate income tax, individual income tax, house and land rent tax and interest tax. Among them, share of the individuals' income tax is in the highest position. Exemption limit and tax rate of the income tax is determined according to the income level and sector wise but is not adjusted according to the inflationary situation of the country and number of dependents. Exemption limit is not provided to the corporate bodies.

The success or effectiveness of income tax system entirely depends upon implementation of provisions, which is the major responsibility of income tax administration. Income tax system of Nepal has been blamed as not enough efficient. Various problems existed in the income tax such as increasing habit of tax evasion,

inefficient income tax administration, defective income tax law are the reasons of lower contribution of income tax. But if we analyze the data relating to it then we can find out that revenue collection from income tax is increasing continuously. Provisions in Act and language have to be made clear. Some reforms in income tax administration are needed to raise the income tax revenue.

Due to reform, the corruption in income tax administration can be decreased, the efficiency and transparency can be improved and the tax administrations will treat the taxpayers as responsible citizen to a considerable extent. The cost of tax collection from taxpayers, government and economy as a whole can be reduced to some extent.

The role of revenue is crucial for the overall development of the country. In this context, the Nepalese government needs to develop a sustainable broad based source of revenue. Since more than 80percent of the total revenue is collected from the tax source, efficient tax system has to be developed and strengthened. In recent years, the government has taken several measures to reduce tax-induced distortions, strengthening tax administration, simplifying tax laws and procedures to make them more transparent. With an aim to broaden the tax base the government enacted new Income Tax Act in 2002. This Tax Act brought all sources of income - from employment, business and investment - under the tax net and helped maintain neutrality of taxation in various income generating activities. The Customs Act was amended to make the Nepalese system compatible with the WTO valuation system, broaden the tax base and mobilize additional revenues by curtailing wide range of exemptions. In 1997, the government introduced VAT aiming to develop it as the backbone of Nepalese Revenue.

### **5.3 Recommendations**

On the basis of this study, the following recommendations are made in order to increase the contribution of income tax in total revenue of government of Nepal.



- a) Tax ratio should be increased gradually on long run basis to meet the deficit in budget. Fro this, the tax base should be widened.
- b) Income tax policy should be formulated according to the economic policy of the country. Income tax policy should be revised timely.
- c) The members involved in formulating income tax policies must have depth knowledge about income tax.
- d) The provisions rewards, prize, incentives should be introduced in the act to encourage the taxpayers to pay tax voluntarily rather through corrective measures.
- e) Tax personnel should be encouraged, punished and transferred on the basis of their work and experience. Regular and effective training system; reward, prize and punishment system should be established for the effective personnel management.
- f) The provisions of fines, penalties and punishments should be made at higher rate for income tax evaders
- g) Income tax, rules and regulation should be clear and simple for all the taxpayers as well as for tax administrators.
- h) The definition made in Income Tax Act should be further clarified and well defined in simple language.
- i) Clear provisions should be made in case of deduction. All the items of deductions should be clearly defined in the act.
- j) To promote export, more deductions should be provided
- k) A research and intelligence centre should be established in each tax office for proper planning and to collect the information in regard to income tax evaders, potential new taxpayers and non-residents who have conducted business without registration.

- l) Separate income tax Department should be established so that the specialization could be achieved in matter of income tax.
- m) Effectiveness of income tax system depends upon the income tax administration. In Nepal, one of the most important reasons for unsound income tax system is inefficient and unscientific income tax administration.

Following recommendations are made for improvement of income tax administration.

- a) Delay in assessment should be reduced as possible for income tax.
- b) Proper tax education should be provided to tax officials as well as tax. Proper tax education should be provided to tax officials as well as tax.
- c) Unnecessary outside pressure should be avoided.
- d) Income tax experts/profession should be increased in tax administration.
- e) The administration should pay great attention to bring the income from house and land rent' doctor's clinics' consultancy service; tuition; research works into income tax net. In these sectors, income tax has been highly evaded.
- f) With a large and growing population of taxpayers it is simply not possible to check the returns filed by every assesses. It is better to proceed on the basis of "self-assessment", subject to random checks. Every taxpayer should be under a credible threat of getting caught for any misstatement.
- g) The habit in business sector of not keeping the complete accounts of the transactions and not submitting the real account for tax assessment must be abolished.
- h) There must me coordination between the departments of tax.
- i) There must be good faith between the taxpayers and the tax collectors.

- j) Effective public participation is necessary to minimize the income tax evasion. Tax authority should do continuous effort in order to develop the taxpayers' positive attitude towards taxation.
- k) There must be partnership between the government and the private sector leadership like FNCCI, CNI etc. in respect of making the taxpayers aware of the taxation.
- l) There are insufficient numbers of tax offices within and outside the Kathmandu valley. Therefore the number of tax offices must be increased to provide the services conveniently.

There has been the problem of collection income tax revenue from a long time in Nepal. The problem can be minimized and income tax will follow a substantial increment in revenue structure of Nepal if the above-mentioned recommendations are managed timely and effectively.

Appendix-A

**Questionnaire to the tax experts, tax payers and tax administration**

Name ..... Designation .....

Office/Organization ..... Occupation .....

1. Are you familiar about income tax? Yes ( ) No ( )
2. Do you consider, that the income tax as a suitable means of raising government revenue?  
  
Yes ( ) No ( )
3. In your opinion, is contribution of income tax to total revenue of Nepal satisfactory?  
  
Yes ( ) No ( )
4. If no, what are the major reasons? (Please rank according to the priorities)
  - a. Defective of income tax act ( )
  - b. Mass poverty and low income level ( )
  - c. Increasing habit of tax evasion ( )
  - d. Inefficient income tax administration ( )
  - e. Inappropriate rate and exemption limit ( )
5. Do you think that contribution of direct tax to total revenue is effective?  
Yes ( ) No ( )
6. Are exemption and deduction provided by act are appropriate?  
  
Yes ( ) No ( )

7. Which income tax assessment method is appropriate in Nepal?
- a. Self-assessment ( )
  - b. Jeopardy Assessment ( )
  - c. Amended Assessment ( )
9. In your thinking, what types of problems are facing by the tax payers while paying income tax?
- a. Consuming unnecessary time ( )
  - b. Expectation illegal incentives by tax personnel ( )
  - c. Vague provisions in income tax laws ( )
  - d. Lengthy process ( )
  - e. Lack of co-operation by tax administrator ( )
10. Are the provisions of fines and penalty under Nepalese tax system reasonable?
- Yes ( ) No ( ) If no, how should it be made reasonable?
- a. By increasing
  - b. By lowering
11. In your opinion, is income tax system of Nepal sound and efficient?
- Yes ( ) No ( )
12. Do you agree that Nepalese income tax administration is effective?
- Yes ( ) No ( )
13. In your opinion, which income tax rate is suitable for Nepal?
- a. Progressive
  - b. Proportional

c. Regressive

14. In your opinion, what is the most important factor for effectiveness of income tax in Nepal to raise government revenue?

a. Clear act, rules and regulation ( )

b. Conscious and honest tax payers ( )

c. Moral and honest tax officers ( )

d. Effective tax administration ( )

e. Political non interruption ( )

f. Others, please specify .....

15. Do you have any other suggestions for achieving effectiveness of income tax in Nepal? If yes, please specify .....

16. Do you think that public awareness program is necessary in Nepal for raising government revenue?

Yes ( ) No ( )

\*\*\*\*\* Thanks for Co-operation \*\*\*\*\*

## Appendix-B

### Composition of tax revenue

Rs. in million

Fiscal year	Customs	Tax on consumption and product of goods services	Land Revenue Registration	Tax on Property and Income	Total
2000/01	12552.1	16153.6	612.9	9546.5	38865.1
2001/02	12658.8	16074.3	1131.8	9465.7	39330.6
2002/03	14236.4	18244.8	1414.3	8691.5	42587.0
2003/04	15554.8	20705.6	1697.5	10215.1	48173.0
2004/05	15701.6	25331.3	1799.2	11272.6	54104.7
2005/06	15344.0	28118.3	2181.8	11787.0	57430.4
2006/07	16707.6	35433.8	2253.5	16726.8	71126.7
2007/08	21062.5	41005.32	2940.32	20147.0	85155.54

Sources: Economic survey 2008/09, MOF

## Appendix-C

### Composition of tax revenue and non tax revenue

Rs. in million

<b>Fiscal year</b>	<b>Tax revenue</b>	<b>Non tax revenue</b>	<b>Total revenue</b>
2000/01	38865.1	10028.8	48893.6
2001/02	39330.6	11115.0	50445.5
2002/03	42587.0	13642.7	56229.8
2003/04	48173.0	48173.0	62331.0
2004/05	54104.7	54104.7	70122.7
2005/06	57430.4	14851.7	72282.1
2006/07	71126.7	16585.8	87712.10
2007/08	85155.54	22467.04	107622.58

Sources: Economic survey 2008/09, MOF



## Appendix-D

### Government expenditure

Rs. in million

Fiscal year	Government expenditure			Total
	Recurrent expenditure	Capital expenditure	Principal payment	
2000/01	45837.3	28307.2	5690.6	79835.10
2001/02	48863.9	24773.4	6434.9	80072.20
2002/03	52090.5	22356.1	9559.5	84006.10
2003/04	55552.1	23095.6	10794.9	89442.60
2004/05	89442.60	27340.7	13533.3	102560.40
2005/06	67017.8	29606.6	14264.8	110889.20
2006/07	77122.40	39729.90	16752.50	133604.60
2007/08	91446.99	53516.1	16386.93	161350.02

Source: Economic Survey 2008/09 MOF.

## Appendix-E

### Government receipts

Rs. in million

<b>Fiscal year</b>	<b>Revenue receipts</b>	<b>Foreign Grants</b>	<b>Total receipts</b>
2000/01	48893.6	6753.4	55647.0
2001/02	50445.5	6686.1	57131.60
2002/03	56229.8	11339.1	67568.9
2003/04	62331.0	11283.4	73614.4
2004/05	70122.7	14391.2	84513.9
2005/06	72282.1	13827.5	86109.6
2006/07	87712.10	15800.80	103512.90
2007/8	107622.58	20320.73	127943.31

Source: Economic Survey 2007/08, MOF.

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