CHAPTER-I

INTRODUCTION

1.1 Background of the Study

The government of a country has to carry out development plans, handle day-to-day administration, maintain peace and security and launch other public welfare activities. The government requires sufficient funds to carry out these activities. To carry out these activities and to fulfill the responsibilities towards the people. The government collects funds from two sources: debt and revenue. The debt can be collected either from internal sources or from external sources. The debt taken from people and institutions within the country by flotation of public debt instruments is known as internal debt. While the funds taken from foreign government, agencies and international institutions are known as external funds or debt. The debt financing is known as deficit financing of the government. The revenues of the government basically come from two sources: tax and non- tax. Tax source includes income tax, custom duty, excise duty, and VAT etc. on the other hand, non- tax includes different revenue like gifts, grants, revenue from public enterprises, administrative revenue such as registration fees, fines and penalties. In Nepal around eighty percent of the government revenue comes from taxation. Therefore tax is the major sources of the government revenue.

Being a Developing country and also just come out from conflict, Nepal is in need of huge amount of capital investment. The government has to make heavy spending for reconstruction of existing as well as in new infrastructure and also for peace, stability and development process. The private sectors of the country are not keen to invest in these activities. Despite infrastructure development, the government also has the need to run several development projects. The expenditures incurred by the state can be fulfilled by two sources: They are internal and external sources.

Internal sources of fund is own source and taken within the nation and the funds taken with foreign government, individuals, institutions and international institutions is known as external fund. Continuous use of external sources of fund to raise necessary public fund is not good because it reduces the liquidity position of the government, increase over-dependence upon other countries and increase the inflation too. So, internal sources are more important and appropriate not only for financing necessary funds but also for proper mobilization of external sources. Internal source has no obligation towards the third party and is less risky compared to the external fund. It is the best source to fund the development activities and can play a vital role in the development process of an economy.

On the other hand, internal source of fund includes both tax revenue and non-tax revenue. Tax revenue includes the amounts which are compulsory contributed by tax payers to the government. They are customs, excise duty, value added tax, corporate and personal income taxes. Nepal gets around 80 percent of the revenue from this source. Non-tax revenue includes different revenues like gifts, grants, special assessment, and revenue from public enterprises, administrative revenue such as registration fees, fines and penalties. In Nepal, around 20 percent of the revenue comes from these sources. Non-tax sources are uncertain and inconvenient because they are imposed according to the necessity of the government. So, taxes are the better sources of public revenue. The use of tax is safer for financing public revenue in developing countries. So, taxation has been taken as the best and effective instruments for raising the government revenue.

External sources of funds are foreign grants and loans which are received from foreign countries, international agencies and organizations. This kind of fund is important for underdeveloped and undeveloped countries. It is used for economic development, reconstruction, foreign exchange and to recover from economic crisis. But external sources are uncertain, inconvenient and not good for healthy development of the nation and decrease the dignity & sovereigns of the people. Like developed and developing countries, Nepal should try to mobilize its internal sources of fund for running the development activities.

Prof. Seligman defined tax as “A compulsory contribution to the government to defray the expenses incurred in the common interest of all without reference to special benefit conferred”.

Plehn defined taxes as “Taxes are general contribution of wealth levied upon persons, natural or corporate to defray expenses incurred in conferring common benefits upon the residents of the states”.

So, a tax is a compulsory levy imposed by the government. It is levied on persons as per the prevailing laws. The person, who pays tax, does not get any direct benefit from the government. It is a compulsory liability of the person who has to pay tax. The collected tax is spent for common interest of the people or it is collected from haves and spent for the interest of have-nots in the society.

Simply, taxes are categorized into two types on the basis form. They are:

- **Direct Tax**
- **Indirect Tax**

If one pays or to be paid tax to the government from his/her own income it is termed as direct tax. Or, direct tax is a tax paid by a person on whom it is legally imposed. And it is a tax on income and property. Examples of direct taxes are: Income tax, property tax, vehicle tax, interest tax, expenditure tax, death tax, gift tax etc.

An indirect Tax is a tax imposed on one person but partly or wholly paid by another. In indirect tax, the person paying and bearing the tax is different. It is the tax on consumption or expenditures. Examples of indirect taxes are: Excise duty, custom duty, VAT etc.

Income tax is a most popular tax. It is considered as one of the major elements of tax revenue. Income tax is charge on person’s income according to the prevailing law of the country. It covers all the fees, additional fees, fines etc. Income includes all the income which is received from employment, business and investment. Income tax is the superior to other taxes because it is imposed on the basis of paying capacity of taxpayers.

“The primary purpose of taxation is to divert control of economic resources from taxpayers to the state for its own use or transfer to other” (Goode, 1980).

In past, the function of the government was limited to maintaining internal law and order and to protect the country and people from foreign aggression or attacks. The collected revenue was use only for the protection of the country and the people. It is said that the rich used to pay more as they required more protection for themselves and their property. Later, the functions of the government widen and also the responsibility of the government was not limited to protect the people and the country only. The government also needs to develop the economy. Economic development could not run only by the private sector. At the same time, the government has to invest in social overheads such as education, health, nutrition, sanitation and economic services like electricity, road, communication, irrigation and so on. The government needs adequate revenue to undertake this function. To fulfill needed revenue, tax was the only easy and appropriate means. In search of easy and more reliable source and to collects more revenue, the income tax came into frame and became more appropriate and reliable source of revenue and ultimately income tax came in the existence. Taxation became the main government instruments to collect maximum revenue in order to pay for the war and to conduct other government activities.

According to income tax Act, 2058, there are two forms of incentives. They are: exemptions of income and deductions of expenses. “An exemption may be in the form of non-taxation of an income or in the form of relief on a payment or expense which is otherwise not allowed or deducted in computing taxable income, profits or gains” (Nagpal, 1960).

The nature of exemptions differs according to the government’s policy and the rules and the regulation of the taxes. Similarly in case of the corporate income tax, the level of tax exemption is dependent with the level of profits earned and size of the corporate body. To encourage the particular business activities the government may decide to allow the tax exemption upto a certain limit or for time period.

Generally, there are two types of equity concept in the taxation. They are: vertical equity and horizontal equity concept. According to vertical equity concept the people with different levels of income must not be taxed at same rate of tax and according to horizontal equity concept the people same levels of income must be taxed at same rate of tax. It seems in many cases, the people with same income level pay different levels of tax because of the difference in the allowance in the different items. It means two taxpayers having the same level of income but earning from the different source have to pay different amount of tax because of different provisions in deductions. On the same regards, the increase in the tax exemption limit sometimes brings conflict with the progressive income tax system. Higher the increase in the exemption limit more benefits for the rich. It can be argued that with the increase in the level of exemption limit the low-income people benefit. The argument is true but the benefits received by the low income taxpayer are proportionally smaller than the benefits received by the high income taxpayers. This is so because of the tax brackets. In general case, the rate of tax is higher for higher incomes. Sometimes, because of the increase on the exemption limit the high income taxpayers' taxable income decreases and due to that they fall in the lower tax bracket and pays taxes at lower rates.

Although, Income Tax Act and Rules have been updated and amended. However, there are many problems about income tax practices in Nepal such as, leakage in tax, people feel about tax as a penalty and burdensome, lack of consciousness of people, lack of mobility of tax administration to cover new taxpayers, delays in computation and collection, lack of accuracy and unity in accounting system, tax avoidance, evasion etc. On the other hand, raising more and more revenue is the main objective of taxation but ultimately affects the pattern of consumption, production and distribution in the economy so, it is necessary to take into account the equity concept to design the proper tax exemption and deduction policy.

1.2 Statement of the Problems

Being a developing country and also just come out from ten years conflict Nepal is in need of huge amount of revenue to invest in existing as well as in new infrastructure and for development process. The government has to make heavy spending on the several social overheads. The funds required to invest for these activities can be obtained from two sources: Internal sources and External sources. The internal source has no obligation towards the third party and less risky as compared to the external sources**.** The external source of fund depends upon the interest and condition of the funding countries.

Nepal has low per capita income as compared to other countries. Because of the low per capita income and low level of income of its people. Nepal is facing difficulties on raising funds from internal sources. Therefore, it is highly depends on the indirect tax than the direct tax. The share of income tax to total revenue is 16.95 percent in fiscal year 2008/09 which is very low, Because of the low level of income and taxpaying capacity of the people. About 30.6 percent of the Nepalese people are said to be under the poverty line and the GDP per capita $ 450 which shows the economic conditions of Nepal. The taxpayers feel burdensome to pay tax in Nepal, because the tax exemption limit is not appropriate and scientific and the deductions provided are not sufficient, there are no benefits offered to the taxpayers as provided in the developed countries. (Economic survey, July, 2009)

Economic growth of the Nepal is very low as compared to neighboring countries. In year 2008 the growth rate of neighboring countries India, Bangladesh, Bhutan, Maldives, Pakistan and Srilanka were 7.3%, 5.6%, 6.6%, 5.7%, 6% and 6% respectively. As compared to this the economic growth rate of Nepal was only just 4.7% and also which expected to decrease in the year 2009 to 3.6% which shows the economic condition of the Nepal. Economic growth is the indicator of the development of the country. But, economic growth of Nepal is not satisfactory i.e. very low economic development and growth. It needs huge amount of capital for the economic development of Nepal. For this, revenue collection should be increased to boost up the economic development. There is still huge resources gap between expenditure and revenue collection. The rate of government expenditure is higher then the rate of revenue collection. The resources gap in fiscal year 2008/09 was Rs. 71367.37 million. This resource gap can be fulfilled by internal and external borrowings. But, external borrowing has played a dominant role to fulfill the resource gap of Nepal, the external borrowing was Rs. 10405.41 million in fiscal year 2008/09. The external borrowings to overcome the expenditure bring the various problems. Internal source is the best source to play a vital role in the development process of the economy. Internal source comprises both tax revenue and non-tax revenue. Tax revenue plays a significant role on the total government revenue of Nepal. The contribution of total tax revenue and non-tax to total government revenue are 80.85 percent and 19.14 percent respectively in fiscal year 2008/09. This shows that the major portion of the government revenue comes from taxation. Although the composition of tax revenue of Nepal shows that the government of Nepal is highly dependent on indirect tax. In fiscal year 2008/09, the contribution of indirect tax to total tax revenue is 72.04%. (Economic survey, July, 2009)

The ratio of the income tax to the GDP and the total tax revenue is very low in our country. While studying the composition of tax revenue. It is observed that there is a dominant share of indirect taxes. The government has to collect more taxes to increase the revenue and perform development activities but low taxable capacity of the people is the constraint. So, this problem can be solved to certain extend by implementing effective tax administration or by the good governance.

As the means of economic growth and social justice, income tax has not succeeded to play significant role in Nepalese tax structure. The contribution of total direct tax and total indirect tax to total tax revenue are 28.95 percent and 71.05 percent in fiscal year 2008/09. It shows that the government is largely depending upon indirect tax. (Economic survey, July, 2009)

Developing countries like Nepal tends to have a greater propensity to evade taxes. Majority of the people are poor and they have no taxable capacity and the major problem of the Nepal is corruption that has been causing to increase the inequality of income and wealth. People have less knowledge about income tax and they have to maintain their livelihood from their limited income. Most of the rich people do not pay tax by using legal loopholes and advantages of an inefficient tax administration and a significant amount of the tax revenue collected goes in the unseen hands of the government expenditure.

There is very poor income tax paying habit of Nepalese people. The tax authorities are inefficient and ineffective in enforcement. There are no integrating programs for taxpayer's education, assistance, guidance and counseling. Tax offices are taken as heaven for corruption harassment and incompetent personnel. The assessment techniques and procedures of income tax is not effective, undue delay in tax assessment by which not only reduces the total revenue, but also brings harassment to the taxpayers. So the coverage of income tax is very narrow in Nepal. Income from employee is taxed more heavily than the capital income and agricultural income is exempted form income tax. These kinds of exemptions encourage and loopholes for tax evasion and complicates to assess to the tax administration.

Income tax Act, 2002, (section 11) has provided some exemptions granted to the special industries and the industries established in the backward areas of Nepal are not effective and scientific. Although tax incentives or concessions encourage or support to establish industries in certain area but they vanish or change name, ownership or place of the business when the tax exemptions and concession period.

Income tax Act, 2002 (section 10) has also provided exemption limit to an individual into two distinct categories in Nepal. They are individual and the couple according to the personal status. This classification does not recognize the various sizes of the dependent family members. There is no discrimination between a taxpayer having only a spouse and a taxpayer with a spouse, parents and children. Therefore this limit in the Nepalese context does not show any specific or definite relationship with per capita GDP as well as with the rate of inflation and poverty norm.

According income tax Act, 2002, the income and expenses which are allowed for deductions are: contribution of provident fund, life insurance premium, the contribution and the investment on the Citizen Investment Fund, Medical expenses, Research and Development, Pollution control cost. Besides these provisions, the tax deductible expenses are the donations made for non-profit earning institutions and other expenses as mentioned above. At present, there is no any provision for deduction on the necessary expenses like the higher education expenses, pregnancy delivery expenses, incurred by the taxpayers for his/her dependents.

However, various problems of exemption of incomes and deductions of expenses can be stated in terms of the following questions:

- Are the contribution of total tax and non-tax revenue to total revenue of Nepal sufficient?
- Is the contribution of income tax to national revenue of Nepal satisfactory?
- Are the exempted items of income and exemption limit being provided by Income Tax Act, 2002, are sufficient?
- Is the tax administration system of Nepal sound?
- Are the current deductions of expenses sufficient?
- What are the major problems and weaknesses of income tax system of Nepal?
- Are the provisions made under the Nepalese Income Tax Act, 2058, sufficient in all respect?

1.3 Objectives of the Study

General objective of the study is to analyze the present system of exemptions of income and deductions of expenses provided by the income tax Act, 2058, and also to provide proper recommendations to build the appropriate tax system so that the government can collect sufficient revenues Which can be used in different types of development and economic activities and increase the income level and living standard of the people. The study also helps to the concerned people to aware about exemptions of incomes and deductions of expenses. Being an opinions survey, the study will analyze the exemptions of incomes and deduction of expenses, which are provided by Income Tax Act. However, main objectives of the study are as follows:

- To analyze the contribution of income tax to national revenue of Nepal.
- To analyze the exemption of incomes and deduction of expenses which are provided by the Income Tax Act, 2002.
- To measure the extent of exemption limit provided to individual and the family and their appropriateness.

- To provide suggestions and recommendations regarding income tax administration and income tax law of Nepal.

1.4 Scope of the Study

The purpose of the study/research is to analyze the exemption of incomes and deduction of expenses provided by the income tax act, contribution of income tax to the government revenue and the extend of exemption limit provided to individual and the family. It also aims to suggest and recommend regarding income tax of Nepal. The geographical area of the study will be Kathmandu valley. The sample space for the opinion will be taken from tax administrator, tax experts/auditor and taxpayer. Considering that the sample taken in Kathmandu valley will represent the nation as a whole.

The scope of the study covers the following aspects of Income tax system of Nepal.

- Contribution of total tax revenue to total government revenue of Nepal.
- Contribution of income tax to the government revenue of Nepal.
- Exemptions of incomes and deductions of expenses.
- Administrative aspects of income tax in Nepal.
- Nepalese tax structure of government revenue.

1.5 Significance of the Study

Nepal being a developing country requires sufficient economical and financial resources for the progress and prosperity. For this, internal and external sources can be used for development activities but the external source of financing is not appropriate rather internal source of financing. In this context, significance of income tax cannot be underestimated in the public finance of a nation. The weaknesses and problems faced by the income tax system should be researched and analyzed objectively to increase the contribution of income tax in the national revenue.

The intensive study on tax exemptions and deductions has not been conducted in Nepal. Even though several scholars doing research on Income Tax has studied tax exemptions and deductions as a minor topic to conduct their research. This study, therefore, is a pioneering effort on the detailed study of tax exemptions and deductions of income taxation in Nepal. In this context, need and significance of this study will be known.

1.6 Limitation of the Study

The present study aims to analyze on exemption of incomes and deductions of expenses in Nepalese Income Tax. It is not a complete study of income tax system in Nepal. The limitation of the study can be stated as follows:

- It is based on exemption of incomes and deduction of expenses but not as a complete study of income tax system.
- The study has covered past 8 years (i.e. from fiscal year 2001/02 – 2008/09).
- Opinions and information from respondents were collected only in the Katmandu valley.
- Opinions of the respondents have been taken as a sense of truth which may not be correct at all time.
- Due to the small sample size, it may not represent Nepal as a whole.
- Both primary as well as secondary data are being used, but the reliability of secondary data has not been examined.

1.7 Organization of the Study

The structure of the study has been organized into five chapters; they are as follows:

I. Introduction.
II. Review of literature
III. Research methodology
IV. Data presentation and analysis
V. Summary, conclusion and recommendations

The first chapter is introduction of the research study which comprises background information, statement of the problems, objectives of the study, scope of the study, need/significance of the study, limitations of the study and organization of the study.

The second chapter is the review of literature. Some books, annual reports of Nepal Rastra Bank, Inland Revenue Department, Ministry of Finance, Statistics Bureau, dissertations, articles, news, magazines and necessarily materials have been reviewed for the study.

The third chapter is research methodology. This chapter comprises research design, population and sample, nature and sample of data, data gathering procedure, data processing procedure and analysis of data, weight of choice and weight of respondents have been described.

The fourth chapter is the presentation and data analysis. This chapter is the major part of the study. This chapter aims to make the critical analysis of income tax system of Nepal with the assistance of authoritative data and opinion survey. In this, tax structure of Nepal, exemptions and deductions of income tax system and an opinion survey have been analyzed. On the basis of analysis, it will try to find out whether the income tax system in Nepal is satisfactory or not. It describes the problems and weakness of tax administration too.

The fifth chapter is mainly concerned with finding, summary, conclusion and recommendations. In the beginning of the chapter, the major findings have been presented about the exemption and deductions of income tax system, tax structure and administration aspects of revenue administration. Some possible areas for reform the defects in income tax system have been recommended.

Bibliography and appendices have been presented in the ending part of the study.

CHAPTER-II

REVIEW OF LITERATURE

2.1 Theoretical Concept

Great Britain is the first country in the world to introduce the modern income tax system. It introduced income tax in 1799 in order o generate revenue of finance the war fought with France.

While the history of income tax was not bright, the situation is different now; Income tax has been an important element of the modern tax system. All sorts of countries have been adopted this tax as an important instrument to generate revenue required to finance state activities. This tax is also considered as fairest tax since it can be tied with the taxable capacity of the taxpayers.

The finance act annually prescribes tax rates classifies some of the procedures mentioned in the income tax act, whereas income tax act governs procedure, penalty and administration of taxes. Hence the provisions and procedures of income tax can be analyzed only by the study of both the income tax exemption and deduction was started since the enactment of the first finance act in 1959 A.D. Since then the tax emption limit and deduction have been revised several times.

2.2 Review of Books

Brief review of different studies has been performed in this research study. The researcher has consultant many books, dissertations, articles, annual reports of different institutes, news, magazines, published and unpublished materials concerning with income taxation during the thesis writing.

While reviewing the books, it was found that most of the books were syllabus wise oriented but some of them have described the problems and prospects of income tax system and a path for reform of income tax. Similarly, most of the dissertations have described the income tax laws, provisions, structure, problems and prospects, contribution of income tax etc. There were no any detailed studies made on the topic of income tax exemptions and deductions. Although, some books of taxation are useful and helpful for this research work which are briefly described below:

Paudyal and Timilsina (1989 A.D.) presented a book of income tax named "Income Tax in Nepal." They described the theoretical as well as practical aspects of income tax. The book was fully based on T.U. syllabus prescribed for B.Com. They did not describe the problems of income tax system and structure of Nepal. The book was descriptive rather than analytical.

Tiwari (1992 A.D.) published a book named "Income Tax System in Nepal." He described the legal provisions relating to income. He described the process, provisions and methods to assess the income with numerical examples. The book was based on T.U. syllabus. Tiwari did not describe the role of income tax in economic development of Nepal and problems of income tax system. His book was descriptive of legal provisions rather than analytical.

Dhakal (2000 A.D.) published a book named "Income tax and House and Compound Tax and Practice with VAT." Dhakal described the legal provisions relating to income tax with numerical examples. This book is very useful to know about legal provisions of income tax Act 1974 A.D. Dhakal was fully based on T.U. syllabus. His book was informative/ descriptive rather than analytical. He did not mention the role of income tax and the structure of income tax.

Adhikari (2003 A.D.) published a book named "Income Tax Law: Then and now." Adhikari described the legal provisions of new income tax Act 2058. Adhikari also described the decisions made by Supreme Court abut the income tax. Adhikari described the legal provisions with critical analysis. His book was very useful to know the new income tax Act 2002 but not analyzed the role of income tax and income tax structure.

Bhattarai and Koirala (2004 A.D.) published a book named "Income Taxation in Nepal with Tax Planning and VAT." This book was published sixth and seventh time in 2007 and 2008 respectively. This book has described the legal provisions with critical analysis. This book has theory and enough practical problems. Critical and comprehensive problems are given. This book also has added income tax act, 2002(as amended by Finance ordinance, 2005) and value added tax Act 1994 (as amended by Finance Ordinance, 2005). This book has also described the tax planning. This book is very useful to know the new income tax Act 2002 with tax planning and VAT but not described the role of income tax and income tax structure.

2.3 Review of Some Articles, Reports

Some articles, reports, were reviewed for this study, which is described briefly below:

Ghimire (1998.) analyzed the principle of direct tax and provision of direct tax. Ghimire described the classification of tax, relation of capital and income, base of income or expenditure tax, procedure of computing income, weakness of traditional accounting system classification of tax rates index, index of income tax in Nepal, contribution of income tax to national revenue, errors of past provisions, reification of tax improvements, etc. Ghimire found that the income tax was only 7% of total revenue that was very low as compared to neighboring countries. For this, he has identified the following causes: No taxation on agricultural income, narrow base of income of retail business, high exemption limit on remuneration income etc. Ghimire accounted the improvement made on income tax like provision of tax collection of source, provision of self assessment of tax, increase in additional fee to remove tax evasion etc. It also described some steps of administrative improvement. They were provision of income assessment committee, flat rate of tax to small taxpayers, establishment of tax offices etc.

Bhattarai (2000.) critically analyzed the income tax facilities provided by Industrial Enterprise Act 1992 in his draft, "Income Tax Facilities provided by Industrial Enterprise Act 1992, an analysis of Rajaswa." Bhattarai described the facilities given to the industries. Bhattarai also critically analyzed these facilities as continuous 7-8 years exemption of income tax would develop the tradition of taking exemption by incorporating legal ways. The deduction allowed on modernization industries, pollution control device, product and technology development, sales promotion expenses etc. would protect only the big industries but not effect to the small industries. Provisions made on advertisement and entertainment or hospitality expenses would create rude on income tax because if it was given to the all industries in the same manner. There was a provision of exemption of income tax of an industry which did not get exemption but reinvested on non-exempted industry. This provision exempts the tax to the industry of alcohol, tobacco etc., if an industry reinvest on non-exempted industry. Periodic exemption of tax would create bad effects such as change in signboard, change in name and change in ownership to own family members.

Kandel (2003) published a draft of Income Tax Act 2002 as a critical analysis. Kandel criticized the ITA 2002 on several grounds such as exemption of agricultural income from income tax, export duties levied on export, inequality between different capital earned income, withdrawal of exemption and adjustment for inflation. Kandel further criticized the act for the provision of income tax from export as 0.5 percent of total export because it is not good choice of income tax base.

Thapa (2004.) published a draft of tax system and its reform in Nepal as a descriptive way. Thapa described the tax system features of tax, causes of reform the tax and areas of reform. Thapa characterized the tax system as high rates, and tax holiday multiple objectives of taxes, too many income brackets and high progressively complicated and ambiguous tax laws:

Thapa identified the areas for reform the tax system in Nepal. They were:

- Simplicity and neutrality,
- Low tax rates on broad base,
- Gradual abolition of exemptions, deductions and to broad tax base,
- Few rates for single rate,
- Few taxes with high revenue productivity,
- Emphasis on tax compliance rather than coercive enforcement,
- Incentives to saving and investment,

- Excise duty only on cigarette, tobacco, alcohol, automobiles, petroleum and automobile spare parts, etc.

Pant (2004) presented an article entitled, "Problems in Tax Administration and their Remedies" published in Journal of Finance and Development. Pant comprehensively explained about the problems and their remedies related with tax revenue. The major types of practical problems and challenges, in tax administration he has mentioned in his article are; showing limited amount of transaction, showing low selling price, lack of issuing and taking bills, lack of showing the real factory cost, commercial fraud, lack of cooperation in tax auditing legal ambiguity and complexity is implementation and lack of coordination between Inland Revenue Department and revenue investment unit. Meanwhile Pant has recommended some valuable suggestions to solve the problems and to overcome the challenges. They are, statistical and information system should be properly managed fixed norms and standards should be used to assess selling price and factory cost, the billing system should be made compulsory, coordination between Inland Revenue Office with various entities, revenue investigation department and its related units should play the important role and auditing of tax should be widened etc.

Kandel (2004, April) presented an article entitled, "Are Tax Incentives Useful?" If so, which one?" published in Journal of Finance and Development. In this article Kandel tried to seek the answer form the survey of various empirical studies earlier done in Nepal, India, Pakistan and other investment countries. Kandel found that the tax incentives are still the controversial matter whether they promote the investment or not. But Kandel argued that most of the developed countries used tax incentives.

As per the studies done in various countries the conclusion in that among different types of tax incentives, investment allowance or investment tax credit and accelerated depreciation are superior to other types of tax incentives. Tax holiday is the most inferior type of tax incentive which causes revenue loss without enhancing the investment environment. Meanwhile, most of the researchers have opposed the tax holiday system both within Nepal and outside Nepal.

Kandel further added that the survey of the studies indicate the accelerated depreciation system had positive impact on investment. The work of reducing tax rate, specially, followed after 1990s to such lowest rate was not a proper decision. That's why if Nepal wants to go to tax incentives again, she should adapt investment allowance or investment tax credit, not the full holiday in future.

In 2010, June, Nagarik daily presented news entitled, “Focuses on Efficiency of Budget Rather Then Size” in this news it tries to present the size of budget for coming FY and revenue collection of last year. In this news it presents the view of representative of industrialist and businessman. One of the representative said that the government should remove the export fees and also demand that the government should give incentives to the export business.

He also added that the exemption limit should be extended to Rs 200000 and Rs 300000 respectively to individual and family or couple. The corporate tax rate should be decreased to 20% from 25% and also the provision of house rent should be changed. The government should collect tax from owner of the house not from the rent payer.

The representative also demands that the VAT should be brought under the multi-rate system. The government should give VAT rebate on agriculture industry, tourism industry, bricks industry and cold storage industry etc.

Pokheral (2010, June), presented an article entitled, “Revenue Increased by 25.83 Percent” published in the rising Nepal daily. In this article he tries to present the significant achievement made by the MOF in revenue collection and mobilization. In this article he presents the growth and mobilization of the government revenue. He presented that in first ten months of FY 2009/10 revenue mobilization of the government grew by 25.83 percent amounting to Rs 138550 million.

He tries to present the efforts made by the government to enhance the revenue mobilization mechanism and make it more effective, the government has taken initiatives to form central revenue board. For this, it had form a recommendation committee and the committee has already submitted its report.

He also presents that the work done by the government to make tax office systematic and efficient. For this the government initiated an innovative work to go for modern and high- tech governance system, the government has prepare e-governance master plan to make electronic system in all the office under inland revenue department with in next five years.

He also present the achievement made by the government by distribution of personal e-pan. The government has already distributed e-pan to 62871 including president Dr. Ram Baran Yadav and Prime Minister Madhav Kumar Nepal.

In this article Pokheral present only the achievement of the government on collection and mobilization of revenue. But he did not analyze and evaluate the collection procedure, rules and regulation of tax system of Nepal, and incentives provided by the government to the tax payer etc.

In 2010 June, Kantipur daily presented news entitled, “Demand to Reduce Corporate Tax Rate” in this news Kantipur reporter tries to present the view of the representative of Nepal Pari Sangh on Nepalese corporate income tax rate. He present that the representative demanded to reduce the corporate income tax rate from 25 percent to 20 percent.
He also presents the view of representative on exempt limit. According to this news the present tax exemption limit is not sufficient and the limit should be extended to Rs 250000 and Rs 300000 respectively to individual and family.

He also present that the government should remove tax on foreign investment gain, VAT should bring under multi- rate system, the government should remove export service fees and also reduce penalties from 25 percent to 10 percent on provision of unable to export.

2.4 Review of Related Studies

Some dissertations and thesis were reviewed for this study. They are as follows:

Regmi (1986) presented a dissertation entitled "The Role of Income Tax in Nepal." Regmi described the conceptual framework of income tax, structure of income tax, income tax and resource mobilization, problems and income tax. Regmi has also described the objectives of income tax. Regmi has given more concentration on the study of tax structure of Nepal. In his study, Regmi found the share of indirect tax was more than 70 percent of total tax revenue in 1981/82. The share of direct tax was about 30 percent of total tax revenue. Within direct tax, the share of income tax was 17.29 percent in 1972/73 which was increased 35.68 percent in 1981/82.

Regmi found the problems of income tax; they were lack of maintaining the record of taxpayer’s assessment delays, lack of responsibility and honesty among the tax officers, tax evasion, corruption, lack of coordination between the various revenue and other non-revenue departments, leakage in personal income tax collection.

Regmi has given suggestions about the income tax were, income tax law should be clear and precise widening the tax coverage, application of scientific assessment method, simple and easy procedure of tax payment, honest and efficient staffs, coordination between staff and departments, establishment of research unit, tax holidays to new industries. Although, Regmi did not mention the legal provisions relating to income tax. His topic was about the role of income tax but he did not describe any role of income tax, any numerical examples and mention the exemption and deduction.

Shivakoti (1987) accomplished a research entitled "Analytical Study of Income Tax in Nepal." Shivakoti presented the concept of income tax along with its historical perspective, role of income tax in Nepal, income tax structure of Nepal, problems of income tax administration in Nepal. Shivakoti also explained that the taxation plays an effective way of mobilizing internal and external sources adequately.

Shivakoti further added that taxation policy in a developing country should include three objectives: First, it should promote saving in the private sector. Secondly, it should reduce wide gap between income of few rich and poorer. Thirdly, it should not have undesirable inhibiting effects in terms of inflationary pressures and it should be or counter inflationary in its action. According to him, income tax plays a vital role for the development of the country. It reduces the unequal distribution of wealth among people and is a suitable method to collect funds. In case bridge the increasing gap of disparity of income. For this purpose, higher income group has to pay more tax and lower income group has to pay less tax.

Shivakoti concluded that income tax has been a pivotal element in direct tax and equally significant for the government revenue in Nepal. But its significance does not seem to have achieved equal attention on the part of the government.

Shivakoti also recommended for a deliberate programme of tax information to awareness to the public so that they can feel that to pay tax is to contribute to the economic development of the country. Likewise, tax administration should be honest, efficient, trained and effective-research unit should be established. Shivakoti further stressed to keep up to date information in tax offices to reduce the delay in the assessment. The personnel working should be encouraged through awarded on the basis of performance and also computer and other scientific equipment should be used.

Baral (1989) carried out a research entitled "Income Tax in Tax Structure of Nepal", T.U. In her study, Baral explained the historical review of tax system, structure of government revenue, contribution of income tax to total tax revenue and total revenue, share of income tax on GDP, total revenue and total tax revenue, Baral found that the share of income tax to total government revenue was increasing i.e. 1.54 percent in 1962/63 and 7.78 percent in 1987/88. But the share of tax revenue to total revenue was 80.79% in 1962/63, which was slightly decreased to 78.89% in 1987/88. The ratio of income tax to GDP was 0.094 in 1964/65 which was increased to 0.76 in

1986/87. Similarly, the ratio of income tax on total revenue was 1.54 in 1962/63, which was increased to 7.787 in 1982/83. So, the ratio of income tax to GDP, total revenue and total tax revenue had an increasing trend but the increasing rate was low as compared to other countries.

Baral has identified the reasons of tax evasion. Which were lack of clear and comprehensive definition of income, lack of proper punishment to tax evaders, tax paying capacity and the consciousness among the taxpayers was low, lack of efficient tax administration, lack of scientific method of tax collection, etc.

Baral suggested that the tax administration should be honest and efficient, tax evaders should be punished, administrative cost should be minimized, research unit should be establishment, delays in tax assessment should be reduced.

Baral also described the tax structure in comprehensive but not identified the major problems of income tax system. Baral did not mention the legal provision relating to income tax and numerical examples. Baral found the reasons of tax evasion but did not describe how could be minimized the tax evasion.

Thapa (1993) conducted a research entitled "Income Tax Assessment Procedure in Nepal, An Analytical Study", T.U. This study was basically concentrated on income tax assessment procedure. His findings about the problems of income tax assessment procedure were adhocism in tax assessment, undue delay in tax assessment and lack of adequate accounting skills, which are considered at present. Thapa conducted an opinion survey of income tax assessment procedure. Thapa took 23 respondents as a sample. About the exemption limit, 6 persons were in positive attitude towards exemption limit, 8 were negative attitude and 9 were indifferent about the exemption limit. Out of them, those respondents gave the negative response, suggested to increase the exemption limit. Thapa suggested to adjust exemption limit according to the inflation of the country. Thapa also suggested to give tax holiday to new industries as investment allowance. Thapa did not mention the assessment procedure legal provision relating to income tax and items of exemptions and deductions.

Acharya (1994) did a research on "income Tax in Nepal" A study of its structure, productivity and problem" T.U. Acharya described the structure of income tax, productivity of income tax and problems of income tax system. He presented some numerical and diagrams of structure and productivity of income tax. His study about income tax was not so detailed because he did not explain the provisions relating to income tax and his study was more concentrated on the problems of income tax system. Although, his findings about the problems of exemption limit and allowances were considerable and accountable. Acharya showed the problems of exemption limit as follows:

- Exemption limit being equal to remuneration taxpayers and business individual does not seem reasonable. The exemption limit for remuneration taxpayers should be comparatively higher than the business individual.
- The exemption limit in the Nepalese context neither shown any definite relationship with per capita GDP nor with the rate of inflation nor with poverty line so it seems to be unscientific. His findings about the problems with allowances were as follows:
    - Fifteen percent depreciation allowances for corporate taxpayers seem to be inadequate.
    - Private boarding schools running now days are basically inclined with profit. They are excluded from income tax, which is not reasonable.
    - One and two percent deduction of the total income from trade, industry, profession and vocational for advertisement and guest hospitality, respectively seem to be low.
    - Allowances for remuneration taxpayers are not scientific in specifying the figure in obsolete term also. Only the proportional figure is recommended, otherwise these should be frequent adjustment in income tax act, which is not so practical.
    - Additional allowances are lacking for specific industries provided that they are feasible in the Nepalese economy. Tourism industries, cooperative organizations in rural sectors etc. are in this category and should been encouraged. On the other hand, the special allowances for export income of industry does not seem essential such as for carpet of

garment industry. It is because those small business investors are unable to export their products.

Tripathee (1995) presented a dissertation entitled "Income Tax System in Nepal and some potential Areas for reforms," T.U. In this study, Tripathee tried to show the tax structure in Nepal, role of income tax in Nepalese economy, income tax administration and tax evasion in Nepal along with reforms.

Tripathee has more emphasized on the income tax administration and tax evasion. Tripathee conducted an opinion survey about the sufficiency of tax incentives and tax holidays to the industries. Tripathee took a sample of 26 respondents, out of them 16 respondents were in positive response and 10 respondents were in negative response about the sufficiency of tax incentives and holidays. According to the respondents following reformatory activities should be performed.

- The industries, who invest Rs. 500,000 or more should be defined as employment oriented industries.
- There should be prize system, which may be as the form of tax incentives or tax holidays to the taxpayers.
- The period of tax holiday should be extended for industry, which utilized Nepalese raw materials and produces handicrafts. The period of tax holidays should be extended 10, 8 and 5 years instead of existing period of 7, 5 and 2 years respectively.
- For the expansion of industry, additional incentives should be provided.
- The items of deduction should be added.

Tripathee suggested should to increase the exemption limit of Res. 25,000 to Rs. 30,000 for an individual, Rs. 35,000 to Rs. 40,000 fore a couple and Rs. 35,000 to Rs. 50,000 for a family

Tripathee's suggestions about deduction of expenses of remigration taxpayers were as follows:

- Expenses for better education of their children not exceeding the amount of Rs. 10,000 pa
- House rent allowances not exceeding Rs. 12,000 p.a.
- Educational expenses for taxpayers himself. If he is studying in an educational institution. His dissertation is very useful to further study about income tax purpose. But he did not include the exempted items of income and business expenses and also not mention about the legal provision relating to income tax system.

Poudyal 'Kshetry' (1998) submitted the Ph.D. thesis entitled, "Corporate Tax planning in Nepal." This thesis report was aimed to examine the implication of tax factors in strategic planning, project planning and optional planning in Nepalese companies. Poudyal found that the majority (90%) of the companies considered tax factors while selecting the line of business. Poudyal also found the positive correlation (+0.8) between tax rate and the debt equity ratio because of interest paid on debt is a tax deductible item. Similarly, the correlation coefficient between average fixed assets and corporate tax was (+0.75) in small companies and (+0.12) in medium size companies. As against this, in large companies, there was a negative correlation (-0.2), which showed that increase the fixed assets in large companies resulted in decrease in the corporate tax. Poudyal addressed that the tax planning should be considered while making corporate planning and such companies should set up separate tax section to get maximum benefit of provisions, provided by tax law. However, tax assessment under the best judgment blocked the application of tax planning in corporate planning. Poudyal has recommended that tax incentives should be given to non-industrial companies too, and tax rate should be differentiated for resident and non-resident companies.

Kandel (2000) presented the Ph.D. thesis entitled, "Corporate Tax System and Investment Behavior in Nepal." He undertook the research work to find out the problems relating to corporate tax, which blocks the development of the private investments. The main objectives of his study were to evaluate the corporate tax system in general to examine the sensitivity of certain policy like inflation, capital gain tax, dividend tax and interest tax etc. based on their impact on tax burden.

Kandel showed the relationship of private investments with average effective tax rate (AETR), Marginal effective tax rate (METR) and tax incentives in Nepal. Kandel found that the METR for debt-financed project are almost negative i.e. (-17%) and positive for equity financed project and debt equity ratio project by 27% and 19% respectively. Kandel has also found the impact of inflation to the METR. According to him, the statutory tax rate deduction had impact on private investments by 60% to 20%. In his regard, he showed the adjusted R^2 value 0.87 at 5% level of significance. Kandel concluded that the statutory tax rate was in moderate level under the financing options: debt mix and equity i.e. it was not much distortive. The relationship between inflation rate and effective tax burden in Nepal was negative.

Shakya (2003) submitted a thesis entitled, "A Study on Income Tax Collection form Commercial Banks." The thesis report was aimed to evaluate the contribution of income taxed paid by commercial banks in the government revenue, point out main income tax related problems faced by commercial banks, analyze relevant options and views of bankers regarding income tax, put forward necessary suggestions and recommendation for income taxation with reference to commercial banks.

Shakya found that during the five years direct tax revenue has contributed 20.01 percent in an average on total tax revenue and it was 79.99 percent of indirect tax revenue. Shakya also pointed out some problems pertaining corporate tax has been found in the course of investigation. Thesis problems are: assessment delay, undue delay in settlement of fixed appeals with revenue tribunal, negative attitudes and behaviour of tax authorities in the time of the payment and clearance and vague provisions which produce disputes. These problems have been affecting in the profitability of banks. Increasing compliance cost and decreasing corporate tax collection. Shakya has recommended that the private investment from domestic as well as from foreign countries should be encouraged so that economic transaction in the national economy would be increased and boosted up when private institutions invest in different sectors, the banking transactions would also be increased and they make higher profits. As a result, corporate tax collections from those sections as well as from other new corporate sectors would be increased. From this, the government has to show the flexibility in making various laws relating to trade, industries and banking to make incentives in order to form new corporate.

Kafle (2004) presented a dissertation named, "Income Tax Contribution from Nepalese Public Enterprises with Reference to Nepal Electricity Authority." Kafle tried to determine to effectiveness of income tax revenue collection from public enterprises and major problems of income tax system and Kafle also tried to find out the contribution of income tax from Nepalese electricity authority to total revenue and total income tax revenue as national revenue of Nepal. Kafle found that income tax on total tax revenue was 8.36 percent in the fiscal year 1993/94 and it increased up to 22.64% in fiscal year 2001/02. Income tax revenue/GDP ratio, income tax revenue/ total tax revenue and income tax revenue/direct tax revenue ratios are 2.2%, 22.64% and 84.02% respectively in the fiscal year 2001/02. The contribution of income tax from Nepal Electricity Authority to total income tax revenue has also been flotation the average contribution is 2.57%. In the composition of income tax from Nepal Electricity Authority on the income tax from public enterprise has shared 8.5% in an average. Lack of clear transparent and progressive economic policy the main reason for unsatisfactory tax collection was due to the lack of effective income tax system of Nepal.

Khatiwada (2004) conducted a research entitled, 'Structure of Income Tax System in Nepal, A Managerial Study". T.U. Khatiwada aimed to evaluate the structure of income tax system and managerial study. Khatiwada accepted that ITA, 2058 and Provisions are difficult to understand, language is vague and unclear, narrow base i.e. agricultural income has not been included in tax net, provision of double taxation in dividend, insufficient provisions related to capital gains.

Khatiwada also analyzed that income tax management system in Nepal is not effective and efficient due to ineffective management system, inadequate government policy and defective income tax laws. Khatiwada also mentioned the major constraints of effective and efficient income tax management system are:

- Misuse of power by tax administrators.
- Less consciousness of tax payers.
- Lack of motivated and trained human resources.
- Inadequate experts in tax management, non-maintenance of books and accounts, time consuming process of income assessment i.e. scientific assessment.

Khatiwada also added income tax assessment procedure is not sound and efficient, high level of evasion found in income tax, income tax administration as a high degree of corruption has been found. But he did not mention any provision about exemption of incomes and deduction of expenses in Nepal.

Niroula (2005) did a research study named, "Study of Incentives and Facilities to Industries, Under Income Tax Act. 2002" T.U. This study was aimed to examine and analyze the effectiveness of tax incentives and facilities to industries. Niroula concluded that;

- Income tax incentives and facilities do not play the major role in the establishment of industries but other factors such as political stability, industrial environment, administrative efficiency and availability of market, raw material, Labour, infrastructure etc play key role in the establishment of industries. If these facilities are available the incentives and facilities provided by the ITA might play major role in the establishment of industries.
- Investment tax credit and investment allowance play vital role in the establishment of new industries.
- A flat rate of 20% income tax to all industries seems to be little bit higher to the small industries.
- The deduction facility of PCC and R & D has been tremendous effect to achieve its objectives and industries are exploiting these facilities.
- Tax rebate of 25% and 30% to the undeveloped and underdeveloped areas are not sufficient.

Niroula has recommended that investment tax credit and investment allowance should be provided to new industries. The rate of 20% to the export industry is higher and it should be minimized. Niroula further recommended that the contradiction between the Income Tax Act and Industrial Enterprises Act should be eliminated. Niroula further conducted from time to time to make aware about the tax incentives and facilities to current taxpayers and potential investors.

Khatiwada (2005) presented the MBS thesis entitled, " Contribution of Income Tax in The Government Revenue of Nepal" he undertook the research work to find out the problem relating to income tax, which blocks collection of the government revenue. The main objectives of the study was to study the historical development of income tax in Nepal, in general to analyze the contribution of direct and indirect tax to total revenue of the government, measure the ability of the income tax to meet the government current requirement, to examine the effectiveness of income tax revenue collection, to analyze the problem of revenue collection from income tax and give suggestion to make income tax effective and efficient.

Khatiwada found that the contribution of tax and non-tax revenue to total revenue of the government was 77.9 percent and 22.1 percent respectively during his study period. He presents the GDP growth rate, tax revenue as percent of GDP were 2.24 percent and 9.88 percent respectively. He found that the direct tax was in decreasing trend and indirect tax was in increasing trend. He found that the income tax was in increasing trend and the amount of income tax in fiscal year 1988/99 was Rs 879.6 million and it increased to 7966.2 million in fiscal year 2002/03. The share of total income tax from public enterprises was 25.50 percent of total income tax. The exemption limit was allowed separately from fiscal year 1979/80 to individual, couple and family before that the exemption limit was same for all categories.

Khatiwada has identified the problems in collection of income tax. Which were lack of effective income tax system, lack of responsible tax administration, lack of proper tax education and training to the tax payer, lack of effective punishment to tax evader, lack of tax paying capacity of the people and consciousness among the tax payer and lack of scientific method of tax collection etc.

Khatiwada suggested to over come from these various problems. He suggested that the terms and procedure under the income tax should be made simple and understandable among the common people, rules and regulation of income tax should be simplified, income tax act should be liberal with broad sense, the government should be launched nationwide campaign to inform people, the government should introduced provision relating to reward, prize, incentives, to encourage the tax payer, the fine and penalties punishment should be made at higher rate to discourage the tax evasion and also to minimize tax evasion public participation should be increased and all the items related to deduction and exemption should be defined clearly in the Act.

Subedi (2009) presented the MBS thesis entitled, “Tax Payer Attitude Towards Exemptions and Deductions under income tax Act 2058” he undertook the research work to find out the problems relating to exemption of incomes and deduction of expenses. The main objectives of the study were to analyze the contribution of income tax to national revenue of Nepal, to examine and evaluate the exemption and deduction facilities provided by income tax act 2002, to examine the view of respondents about the exemption and deduction facilities provided in the present tax Act and provide suggestion and recommendation to the income tax administration and income tax law.

Subedi found that there was highly resource gap in Nepal, income tax is the major source of the government revenue, contribution of income tax to total revenue is in increasing trend, tax GDP ratio is not satisfactory as compare to other developing countries, the exemption limit for all tax payer was equal from fiscal year 1965/66 to 1966/67 which was Rs 5000, which was divided into three categories in fiscal year 1978/79. He found that the exemption limit was increased according to time and situation which was Rs 125000 and Rs 140000 during his study period which he found that not sufficient and also the provision of deduction facilities provided by income tax Act was not sufficient.

Subedi found that the main causes for the creation of ineffective tax administration were weakness in government’s policy, less public participation, defective income tax

Act, lack of trained employee, faulty organization structure of tax administration, shortage of tax experts/ professional in tax administration etc.

Subedi also found that the exempted items mention in the income tax Act 2002 insufficient and inappropriate for all categories. Current additional tax exemption limit (30,000, 24,000, 18,000, 12,000 and 6,000 to A, B, C, D and E areas respectively) to the individual working in remote areas is proper or suitable. The medical facilities provided to an individual is not proper or appropriate. And lastly he found that as a whole the provision of exemptions and deductions made under the income tax act 2002 are insufficient in all respects.

Subedi suggested to increase the exemption limit to Rs 150000 to individual and Rs 200000 to family or couple. He suggests to replace the additional exemption given for some period to encourage establishing industries in different remote areas by introducing separate special package. He also suggested to be brought into tax net to non- transparent tax exempted organization by making separate law and rules.

Subedi also suggested on deduction of expenses which were as follows:

- Clear provision should be made regarding deductions of expenses.
- Items of deduction should be defined clearly.
- Due to unclear provision gives double meaning and which creates loopholes, it should be reduced from Act,
- Donation up to Rs 50 lakh given before six month until election to the political parties registered in the election commission should be eliminate from tax Act.
- Actual medical expenses made by tax payer should be allowed for deduction.
- Whole interest expenses should be allowed for deduction within fiscal year.

Acharya (2009) presented MBS thesis entitled, “A Study on VAT: Trend Analysis and Projection”. He undertook the research work to find out the problem relating to collection of VAT and income tax, which blocks the reform of income tax system in Nepal. The main objective of his study were to review the theoretical aspects of VAT, analyze the trend of total government revenue, analyze the trend of total tax revenue, analyze and evaluate the trend of VAT and give suggestion for the improvement of VAT and income tax system in Nepal.

Acharya found that the VAT was implemented to the purpose of rectifying the problems within the existing tax system. He found that the VAT was the replacement of sales tax, contract tax, entertainment tax and hotel tax. He found that the VAT was implemented after excising the various programs such as publicity, campaigns, workshop training, publication of articles, discussion on radio and television etc. he found that for implementing the VAT only the positive aspects of VAT were discussed and published but the negative aspects were not consideration. Therefore, there was problem to implement the VAT successfully.

Acharya also found that the revenue collection from VAT is less then tax collected from tax which was replaced by VAT in earlier years i.e. collection from four taxes that have been replaced by VAT were maximum of 35 percent and minimum of 33.2 percent in fiscal year 1990/91 and 1996/97 respectively of the total tax revenue. As compare to this after the implementation of VAT 30 percent of total tax revenue. He found that the contribution of total government revenue, total tax revenue and non-tax revenue were in increasing trend and also in future the contribution from VAT to the total revenue seems to be increasing.

Acharya has identified the reason for low collection of revenue from VAT and income tax. Which were lack of sound VAT and tax administration, lack of motivated tax administration, lack of honest tax payer and supportive tax administration, lack of awareness, improper billing system, under valuation of bills, smuggling in boarder side and lack of proper preparation work of the government.

Acharya suggested that the government should make tax administration effective, supportive and honest. He suggest that the government should bring strong programmed to tackled with the smuggling in the border side. He suggested that the existing exemption has board coverage and it should be minimized successfully. He also suggested that due to too many tax shelters with series of tax exemption and deduction must be eliminated that have not only disturbed the tax structure but also led to massive corruption.

2.5 Summing Up

During the research study, the researcher viewed various books, reports, articles and dissertations and thesis. Most of the researchers are concerned on the legal and assessment procedure of income tax, administrative and historical aspect of income tax. The thesis and dissertations presented by the researcher have focused about the trend of income tax collection and tending to rise of income tax with GDP, inefficiency of tax administration, widespread of tax evasion, value added tax, role of income tax income tax system in Nepal, problems and prospects of income tax in Nepal, corporate tax planning of Nepal, income tax collection from commercial banks etc. There is a limited number of research studies carried out specifying tax payer groups and concentrated on exemption and deductions of income tax. No attention is paid on a particular problem like exemption of incomes and deduction of expenses. Most of them have been taken various problems as their research objectives and no thoroughly study on a particular subject problem. The researcher has found that no more study done in exemption of incomes and deduction of expenses. This study will help to know the provisions of exemptions and deductions provided by ITA, 2002 and getting optimum benefits within the frame of ITA by exempting of incomes and deducting of expenses to the taxpayers.

CHAPTER-III

RESEARCH METHODOLOGY

This chapter describes the methodology used in this study by covering the procedure of getting research problems as per the objectives. In other words, research methodology describes the methods and processes applied in the entire aspect of the study. Opinion survey technique is used to gather the primary data about different aspects of income tax. While conducting opinion survey, questionnaire were distributed to different groups who were belonged to income tax. They were taxpayers, income tax experts, income tax administers etc. The secondary data are collected from the published and unpublished of different organizations and agencies.

3.1 Research Design

Research Design is a plan, structure and strategy of investigation so as to answer to research questions. This research study attempts to analyze the present exemption and deduction of income tax, the primary information i.e. opinion of the respondents as well as secondary information's were used to analyze the study. The opinion of 50 respondents associated with the income tax Viz. Income tax policy makers, administrator, experts and payers were collected from questionnaire. The questionnaire includes the problem of income tax administration, soundness of income tax administration, exempted incomes, exemption limit, deduction of expenses, sufficiency of provisions, weaknesses associated with that current income tax, etc. In this way, the research methodology applied in this study can be taken as descriptive as well as analytical research design.

3.2 Population and Sample

Population refers to the entire group of people, organizations, events of interest that the researcher wishes to investigate. Similarly, sample is a collection of items or elements from a population which represents as a whole. Hence, a sample is only a portion or subset of the population. It comprises some observations selected from the population. In this study, population comprises all persons belonging to income tax of Nepal. 50 samples from Kathmandu valley have been taken to fulfill the objective of the study. The respondents have been divided into 3 groups. The following table shows the group of respondents and the size of sample.

Table 3.1 Group of Respondents and Size of Sample from Each Group

S.N.	Group of Respondents	Sample Size
1	Income Tax Experts	10
2	Income Tax Administrators	20
3	Income Tax Payers	20
Total Respondents		50

3.3 Nature and Source of Data

The data used for this study were collected from the primary and the secondary sources. The primary data were collected from primary sources. The primary sources of data were the opinion survey through questionnaire, field visit and interview with the respondents.

The secondary data were colleted from secondary sources. The secondary sources of data are the information received from books, journals, newspapers, annual reports, economic surveys, budget speech etc. The major source of secondary data are as follows:

- Annual reports of IRD/N of different years.
- Economic surveys and Budget speeches of various years, published by Ministry of Finance (MOF), Nepal.
- Reports from central Bureau of Statistics.
- Statistical Abstracts, published by MOF Department of Taxation of Nepal.
- Books, News, Journals etc related to income tax.

3.4 Data Gathering Procedure

The required data for this study were collected from two sources Viz. Primary sources and secondary sources. The primary data were collected by using questionnaire and interview methods. A set of questionnaire was developed and distributed to the selected respondents and some of the information was also collected from interview with the respondents in order to get actual and accurate information.

The secondary data were collected from the publication of different organizations and reports, news, bulletin, abstract, journals, budget speeches and economic surveys were also used for the secondary data.

3.5 Data Processing Procedure and Analysis of Data

The data from primary and secondary sources are tabulated initially into distinct format. The data are tabulated into various tables and figures according to the subject in order. Then sample statistical analysis like percentage and rank are calculated where necessary and they have been presented and analyzed in descriptive way. Graphs and charts are also presented to interpret visually the findings of the study.

3.6 Weight of Choice

The respondents are requested to give their opinion on the objective answer or to give yes/no response. While ranking the answer, the rank may be varying from one question to another. The rank is given according to the numbers of probable answers. For example, if the probable answer is 10, the scale/rank was given 1 to 10 where 1 stands the most important and 10 is the least important. The total points obtained by each choice is converted into percentage. The choice having lowest percentage is ranked as the most important and the choice having highest percentage is ranked as the least important.

CHAPTER- IV

PRESENTATION ANDANALYSIS OF DATA:

4.1 Tax Structure of Nepal

Modern economic development of Nepal was started with the initiation of first economic planning in 1956 A.D. Since then, taxes have been used for the achievement of national economic goals. So, taxes play vital role for the economic development of Nepal. Tax structure should be known to study about the taxes. Tax structure refers to the level as well as relative importance of various taxes in the composition of total tax revenue of a country. Tax structure of any country is composed of both direct and indirect taxes.

4.1.1 Composition of Total Revenue

Total revenue in Nepal is composed of from both tax and non-tax revenue. Tax revenue includes income tax, house and land registration fees, vehicle tax, interest tax and VAT etc. Non-tax revenue includes charges, fees, financial forfeiture, receipts from commodities and services, royalty and sale of fixed assets etc. the composition of total revenue of the government from fiscal year 2001/02 to 2008/09 is given in the table 4.1 which is as follows:

Table 4.1 Composition of total revenue

(Rs in Million)

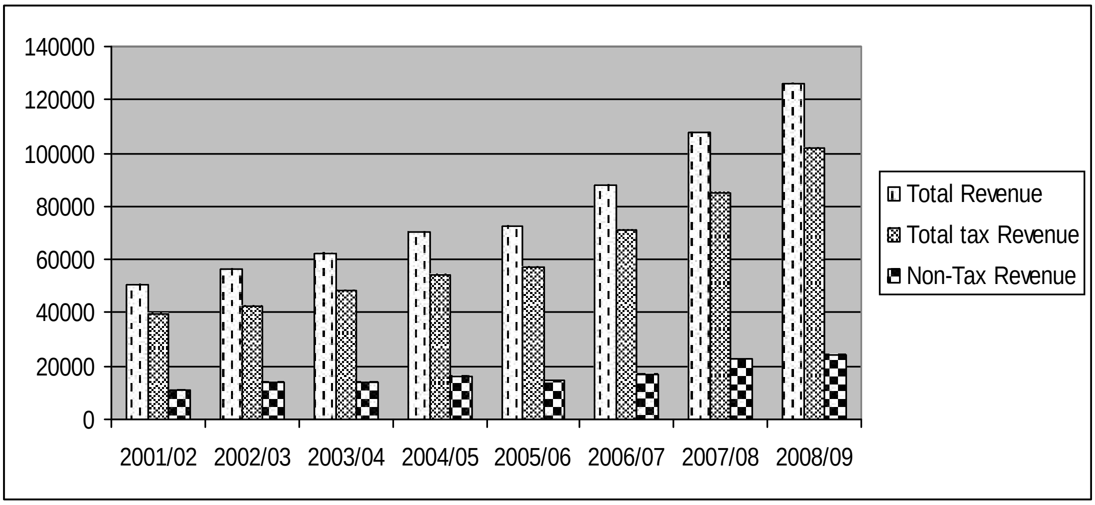
Fiscal year	Total Revenue	Total tax Revenue	Tax Revenue as % of Total Revenue	Non-Tax Revenue	Non-Tax Revenue as % of Total Revenue
2001/02	50445.54	39330.50	77.97	11114.90	22.03
2002/03	56229.70	42586.00	75.74	13642.86	24.26
2003/04	62331.00	48173.00	77.28	14158.00	22.72
2004/05	70122.70	54104.70	77.16	16018.00	22.84
2005/06	72282.00	57430.40	79.45	14851.60	20.55
2006/07	87712.20	71126.70	81.09	16585.50	18.91
2007/08	107622.50	85155.54	79.12	22467.04	20.88
2008/09	126304.80	102120.30	80.85	24184.50	19.15
Total	633050.40	500027.10	-	133022.40	-
Average	79131.30	62503.38	78.98	16627.80	21.02

Source: Economic survey July, 2009

Table 4.1 shows that the composition of the total government revenue. In 2008/09 the contribution of non-tax revenue is 19.15 percent of total revenue as compare to 22.03 percent in FY 2001/02. On the other hand, the contribution of total tax revenue to total revenue in FY 2001/02 was 77.97 percent and it was increased to 80.85 percent in FY 2008/09. The contribution of the total tax revenue and non- tax revenue seems to be fluctuating in between 77 percent to 81 percent and 18 percent to 25 percent respectively during the study period of eight years. The total tax revenue, non-tax revenue and total revenue were Rs 102120.3 million, Rs 24184.5 million and Rs 126304.8 million respectively in FY 2008/09 which was grater then the FY 2001/02. Where as the average percentage contribution to total revenue were 78.98 percent and 21.02 percent i.e amounting to Rs 62503.38 million and 16627.80 million respectively during the study period of eight years. The tax revenue contributes almost four times more than the non- tax revenue. Therefore tax revenue plays the vital role in total revenue of the government of Nepal.

The composition of tax and non- tax revenue to total revenue is shown in the following figure.

Figure 4.1 The contribution of tax and non-tax revenue to total revenue



4.1.2 Composition of Total Tax Revenue

Total tax revenue is composed of from both direct and indirect tax revenue. Tax revenue is the sum of total direct and total indirect tax revenue. Direct tax revenue includes income tax, property tax, interest tax, vehicle tax and gift tax etc. on the other hand, indirect tax includes VAT, excise duties, import and export duties etc. the composition of total tax revenue is given in the following table:

Table 4.2 Contribution of direct and indirect tax to total tax revenue

(Rs in million)

Fiscal year	Total Tax Revenue	Total Direct Tax	Direct Tax as % of Total Tax Revenue	Total Indirect Tax	Indirect Tax as % of Total Tax Revenue
2001/02	39330.64	10597.55	26.94	28733.10	73.06
2002/03	42586.92	10105.66	23.73	32481.20	76.27
2003/04	48173.00	11912.60	24.73	36260.40	75.27
2004/05	54104.70	13071.8	24.16	41032.90	75.84
2005/06	57430.40	13968.10	24.32	43462.30	75.68
2006/07	71126.70	18980.30	26.69	52146.40	73.31
2007/08	85155.54	23087.76	27.12	62067.82	72.88
2008/09	102120.30	29571.30	28.96	72549.00	71.04
Total	500028.20	131295.10	-	368733.10	-
Average	62503.52	16411.82	26.26	46091.63	73.74

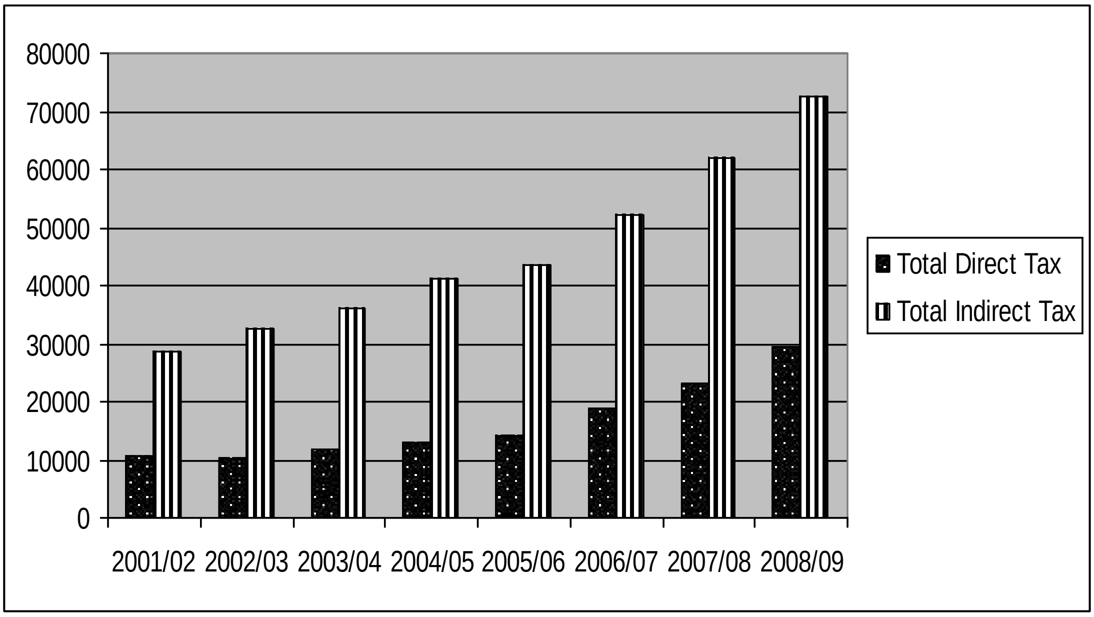
Source: Economic survey July, 2009

Table 4.2 shows that there has been simultaneous increased in the amount of direct tax, indirect tax and total tax revenue in the absolute term. In FY 2001/02 the amount were Rs 10597.55 million, Rs 28733.10 million and Rs 39330.64 million respectively. This amount increased to Rs 29571.30 million, Rs 72549.00 million and 102120.30 million in the FY 2008/09. Despite the increment of amount of the direct tax and indirect tax, their contribution to total tax revenue was fluctuating in between 23 percent to 29 percent and 71 percent to 77 percent respectively. The contribution of direct tax to total tax revenue was 26.94 percent in FY 2001/02 amounting to Rs 10597.55 million and decreased to 23.73 percent in FY 2002/03 and then it started to increase and reached to 28.96 percent amounting to Rs 29571.30 million in FY 2008/09. On the other hand, the contribution of indirect tax to total tax revenue was

73.06 percent in FY 2001/02 and increased to 76.27 percent in FY 2002/03 after that it started to decreased and come down to 71.04 percent in FY 2008/09 amounting to Rs 72549.00 million. The average collection of total tax revenue, direct tax revenue and indirect tax revenue were Rs 62503.52 million, Rs 16411.82 million and 46091.63 million respectively during the study period of eight years and the average percentage contribution of direct tax and indirect tax revenue to total tax revenue was 26.26 percent and 73.74 percent respectively.

The following figure shows the percentage contribution of total direct and indirect tax to total tax revenue:

Figure 4.2 Percentage contribution of total direct tax and indirect tax to total tax revenue



4.1.3 Contribution of Various Taxes as Percent to GDP

The contribution of various taxes as percent to GDP is given in the following table:

Table 4.3 Contribution of various taxes as percent to GDP

Fiscal year	TR	TTR	DT	IDT	IT	Custom duty	Excise duties	VAT	LRRF
2001/02	11	8.60	2.61	6.28	1.94	2.76	0.83	2.68	0.24
2002/03	11.40	8.70	2.31	6.63	1.62	2.90	0.97	2.74	0.28
2003/04	11.60	9	2.51	6.77	1.72	2.90	0.89	2.70	0.31
2004/05	11.90	9.20	2.38	6.97	1.73	2.66	1.09	3.21	0.30
2005/06	11.10	8.80	2.31	6.65	1.58	2.35	0.98	3.31	0.33
2006/07	12.10	9.80	2.61	7.18	2.07	2.21	1.28	3.59	0.31
2007/08	13.20	10.40	2.82	7.58	2.11	2.57	1.36	3.64	0.35
2008/09	14.80	12.20	3.53	8.67	2.55	2.76	1.65	4.25	0.48

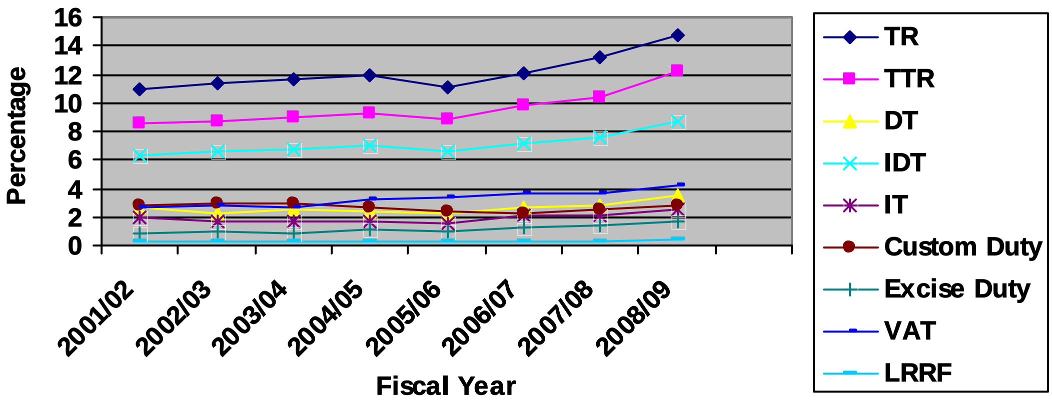
Source: Economic survey July, 2009

Above Table 4.3 shows that the contribution of total revenue to GDP in FY 2001/02 was 11 percent and which was increased to 14.8 percent in the FY 2008/09. The contribution of total revenue to GDP was in increasing trend till FY 2004/05 and in FY 2005/06 it decreased to 11.10 percent. After that it again started to increase and reached to 14.80 percent in FY 2008/09. In over all the contribution of total tax revenue to GDP was in increasing trend. In FY 2001/02 the contribution of total tax revenue to GDP was 8.6 percent which is increased to 12.2 percent in FY 2008/09. Within the total tax revenue, there was significant role of indirect tax which contributes almost three times more then direct tax. In FY 201/02, the contribution of indirect tax and direct tax were 6.28 percent and 2.61 percent respectively and which are increased to 8.67 percent and 3.53 percent in FY 2008/09.

The contribution of income tax to GDP was increased gradually. It contributes 1.94 percent in FY 2001/02 which was increased to 2.55 percent in FY 2008/09. The contribution of land revenue and registration fees was 0.24 percent and 0.48 percent respectively in FY 2001/02 and FY 2008/09. Which was in fluctuating trend, In FY 2001/02 it was 0.24 percent and it increased to 0.31 percent in FY 2003/04 and decreased to 0.30 percent in FY 2004/05 and after that it started to increased and reached to 0.48 percent in FY 2008/09.

The contribution of custom duty to GDP was higher then other individual indirect tax. The contribution of custom duty to GDP in FY 2001/02 was 2.76 percent it was in fluctuating trend. In FY 2003/04 it was increased to 2.90 percent and then started to decreased and come down to 2.76 percent in FY 2008/09. The contribution of VAT was in increasing trend it contributes 2.68 percent in FY 2001/02 which was increased to 4.25 percent in FY 2008/09. The contribution of excise duties to GDP was 0.83 percent in FY 2001/02. In FY 2002/03 it increased to 0.97 percent and it was in fluctuating trend till FY 2005/06 after that it started to increase and reached to 1.65 percent in FY 2008/09. The following figure shows the contribution of various taxes as percent to GDP

Figure 4.3 Contribution of various taxes as percent of GDP



4.1.4 Composition of Indirect Tax

Nepalese tax revenue is dependent mainly on indirect tax. The main portion of tax revenue is covered by indirect tax i.e. indirect tax is almost three times more then other tax. Therefore the Nepalese tax structure is heavily dependent on indirect taxes. Which contributed 71.04 percent to total tax revenue in FY 2008/09.

The major components of indirect tax in Nepalese tax structure are custom duty, excise duties and VAT etc. custom duty is composed of from import and export duty. Custom duty and VAT are the main components of indirect taxes. The major components and their relative percent to indirect tax are given in the following table:

Table 4.4 Major components of indirect tax and their relative percent to the indirect tax

(Rs in million)

Fiscal Year	Total Indirect Tax	Custom Duty	As % of IDT	Excise Duties	As % of IDT	VAT	As % of IDT
2001/02	20733.10	12658.75	44.06	3807.05	13.25	12267.30	42.69
2002/03	32481.20	14236.43	43.83	4785.12	14.73	13459.70	41.44
2003/04	36260.40	15554.80	42.90	6226.70	17.17	14478.90	39.93
2004/05	41032.90	15701.60	38.27	6445.90	15.71	18885.40	46.02
2005/06	43462.30	15344.00	35.30	6507.60	14.97	21610.70	49.73
2006/07	51214.40	16707.60	32.03	9343.20	17.91	26095.60	50.06
2007/08	62067.82	21062.50	33.39	11189.58	18.02	29815.70	48.05
2008/09	72549.00	23105.85	31.84	13831.95	19.06	35611.20	49.10
Total	359801.1	134371.5	-	62137.1	-	172224.5	-
Average	44975.13	16796.43	37.35	7767.14	17.26	21528.06	45.39

Source: Economic survey July, 2009

The Table 4.4 reflects that the major portion of indirect tax was occupies by the VAT and custom duty. Total indirect tax collected in the FY 2001/02 was Rs 28733.10 million of which Rs 12267.30 million i.e. 42.69 percent was contributed by VAT and 44.06 percent amounting to Rs 12658.75 million was contributed by custom duty and the contribution from excise duties was 13.25 percent amounting to Rs 3807.05 million.

The percentage contribution of custom duty to total indirect tax was in fluctuating trend from FY 2001/02 to FY 2006/07 which was 44.06 percent in FY 2001/02 and 32.03 percent in FY 2006/07 and it was increased to 33.93 percent in FY 2007/08. But again in the FY 2008/09 it decreased to 31.84 percent.

The contribution of VAT was also in fluctuating trend. But the amount of VAT was in increasing trend during the study period of eight years. The amount of VAT in FY 2001/02 was Rs 12267.30 million i.e. 42.69 percent which was increased to 49.73 percent in FY 2005/06 amounting to Rs 21610.70 million. The maximum percentage contribution of VAT was in FY 2006/07. But the maximum amount of contribution of

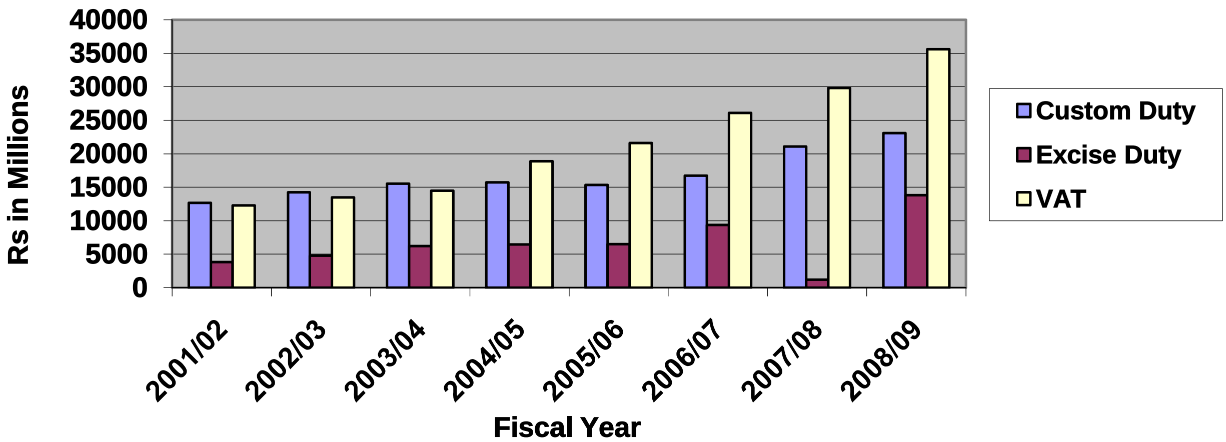
VAT was in the FY 2008/09 i.e. Rs 35611.2 million. Such significant increase in VAT indicates the improvement in the consumption of the Nepalese people.

The contribution of excise duties to total indirect tax was in increasing trend till the FY 2003/04. This was 13.25 percent in FY 2001/02 and increased to 17.17 percent in FY 2003/04. After that it started to decreased and down to 14.97 percent in FY 2005/06. Again from FY 2006/07 it started to increased and reached to 19.06 percent in FY 2008/09. However the amount of excise duty was in increasing trend i.e. Rs 3807.05 million in FY 2001/02 and increased to Rs 13831.95 million in FY 2008/09

The average collection of custom duty, VAT and excise duty were Rs 16796.43 million, Rs 21528.06 million and Rs 7767.14 million respectively during the study period. The average percent contribution of custom duty, VAT and excise duties were 37.35 percent 45.39 percent and 17.26 percent respectively.

The following bar diagram shows the components of indirect tax and their contribution to total indirect tax:

Figure 4.4 Major components of indirect tax and their contribution to total indirect tax



4.1.5 Composition of Total Direct Tax

The major components of direct tax are income tax, urban house and land rent tax, house and land registration tax, interest tax and other tax etc. interest tax and urban house and land rent tax were included under the income tax from the FY 1994/95. Thus the contribution of income tax become larger then other individual direct taxes. The components of direct tax and their contribution to the direct tax is given in the following table:

Table 4.5 Components of direct tax and their relative percent to total direct tax

(Rs in million)

Fiscal Year	Direct Tax	Income Tax	As % of DT	Vehicle Tax	As % of DT	HRLRT	As % of DT	Others Tax	As % of DT
2001/02	10597.55	8903.7	84.16	559.74	5.28	1131.82	10.68	-	-
2002/03	10105.66	7966.20	78.82	559.48	5.53	1414.70	14	165.77	1.65
2003/04	11912.6	9245.9	77.62	700.60	5.88	1697.50	14.25	268.60	2.25
2004/05	13071.80	10159.4	77.72	806.50	6.16	1799.20	13.76	306.70	2.36
2005/06	13968.10	10373.7	74.27	847.60	6.06	2181.10	15.61	565.70	4.06
2006/07	18980.30	15034	79.20	935.00	5.24	2253.50	11.87	697.80	3.69
2007/08	23087.76	17311.2	74.98	1069.21	4.63	2940.40	12.73	1766.6	7.66
2008/09	29571.30	21418.	72.42	1884.60	6.37	4084.74	13.81	2184.6	7.4
Total	131295.10	100412.1	-	7362.73	-	17502.96	-	5955.77	-
Avg.	16411.88	11651.52	77.39	920.84	5.65	2187.87	13.33	744.47	4.15

Source: Economic survey July, 2009

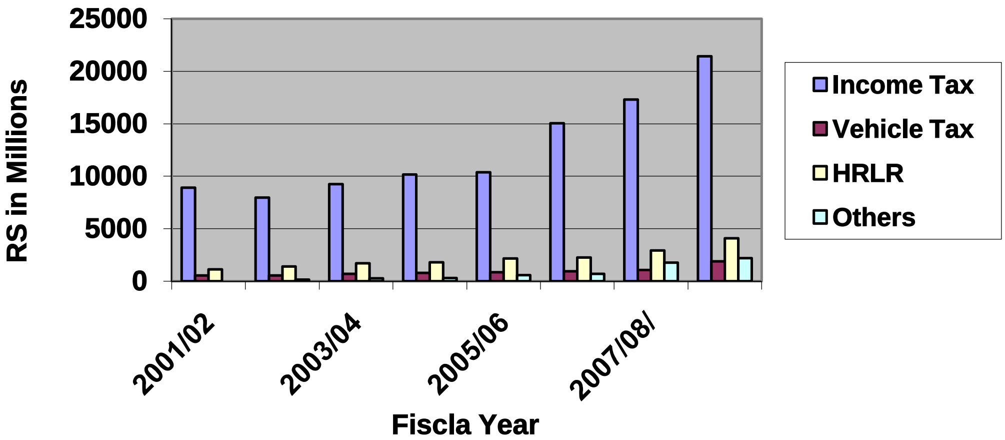
From the Table 4.5 it can be seen that income tax occupies the major portion of total direct tax and the percentage contribution of income tax to total direct tax in FY 2001/02 was 84.01 percent amounting to Rs 8903.70 million. It was in fluctuating trend. In FY 2003/04 it decreased to 77.62 percent and increased to 77.22 percent in FY 2004/05. After that it further decreased to 774.27 percent in FY 2005/06. In FY 2006/07 it increased to 79.20 percent. In FY 2008/09 its contribution was 72.42 percent which was the minimum contribution during the study period. But the amount of income tax was in increasing trend from FY 2002/03 to FY 208/09 i.e. Rs 7966.20 million to Rs 21418.05 million.

The contribution of vehicle tax to total direct tax in FY 2001/02 is 5.28 percent amounting to Rs 559.74 million. The percentage contribution of vehicle tax was in fluctuating trend. But the amount of vehicle tax was in increasing trend. The percentage contribution of vehicle tax till FY 2004/05 was in increasing trend i.e. 5.26 percent in FY 2001/02 and increased to 6.16 percent in FY 2004/05. After that it decreased to 4.63 percent in FY 2007/08. In FY 2008/09 the contribution of vehicle tax to total direct tax 6.37 percent amounting to Rs 1884.6 million.

The contribution of house and land registration fees and other tax were 14 percent and 1.65 percent in FY 2002/03. The contribution from these taxes were in increasing trend till FY 2005/06 i.e. 15.61 percent and 4.06 percent respectively in FY 2005/06. After that the contribution from these taxes had been decreased to 11.87 percent and 3.69 percent respectively in FY 2006/07. In FY 2008/09 the contribution of these taxes were 13.81 percent and 7.4 percent respectively. The average percentage contribution of income tax, vehicle tax, house and land registration fees and other taxes were 77.39 percent, 5.65 percent, 13.33 percent and 4.15 percent respectively.

The components of direct tax and their contribution to total direct tax is shown in the following figure:

Figure 4.5 The components of direct tax and their contribution to total direct tax



4.1.6 Contribution of Direct Tax

The contribution of direct tax to total revenue, total tax revenue and GDP is shown in the following table

Table 4.6 Contribution of total direct tax to total tax revenue, GDP and total revenue

(Rs in million)

Fiscal Year	Total Direct Tax	DT As % of Total Tax Revenue	DT As % of GDP	DT As % of Total Revenue
2001/02	10597.55	26.94	2.61	21.00
2002/03	10105.66	23.73	2.31	17.97
2003/04	11912.60	24.73	2.51	19.11
2004/05	13071.80	24.16	2.38	18.64
2005/06	13968.10	24.32	2.31	19.32
2006/07	18980.30	26.68	2.61	21.63
2007/08	23087.76	27.12	2.82	21.45
2008/09	29571.30	28.95	3.53	23.41
Total	131295.10	-	-	-
Average	16411.89	25.83	2.63	20.32

Source: Economic survey July2009

From the Table 4.6 it can be seen that the contribution of total direct tax to total tax revenue was 26.94 percent in FY 2001/02 and decreased to 23.73 percent in FY 2002/03. After that it was in fluctuating trend till the FY 2004/05 and then started to increase from the FY 2005/06 i.e. 24.32 percent and reached to 28.95 percent in FY 2008/09.

The contribution of total direct tax to total tax revenue was not satisfactory very low as compare to indirect tax. It was because of the exemption of income given to the agricultural sector.

The contribution of total direct tax to GDP was very low. Its contribution in FY 2001/02 was 2061 percent and it was decreased to 2.31 percent in FY 2002/03 and in FY 2003/04 increased to 2.51 percent. The contribution of total direct tax to GDP was in fluctuating trend during the study period. Its contribution to GDP in FY 2008/09 was 3.53 percent which was the maximum during the study period. On the other hand, the contribution of total direct tax to total revenue remained in between 17 percent to 24 percent during the study period of eight years. In FY 2001/02 its contribution to total revenue was 17.97 percent and increased to 23.41 percent in FY 2008/09. The average percentage contribution of total direct tax to total tax revenue, GDP and total revenue were 25.83 percent, 2.63 percent and 20.32 percent respectively.

4.1.7 Contribution of income tax in Nepal

Nepal has started delay in practicing of income tax. Income tax was imposed as on business profit and remuneration tax in FY 1959/60. Since then it has contributed revenue to the nation. In the beginning of this tax, it contributed Rs 203 thousand as revenue in FY 1959/60 (budget speech 1960/61). Income tax was initially levied on business profit and remuneration tax. In 1962 the first income tax Act was enacted which replace the business profit and remuneration tax. After the introduction of new act the contribution of income tax was increased 10 tomes more then the previous years. In present it is the most powerful and important tools to generate the government revenue of Nepal. The following table shows the contribution of income tax on different revenue heads from FY 2001/02 to FY 2008/09:

Table 4.7 Contribution of income tax to different revenue heads

(Rs in million)

Fiscal year	Income Tax	IT as % of DT	IT as % of TTR	IT as % of TR	IT as % of GDP
2001/02	8903.70	84.01	22.63	17.65	1.94
2002/03	7966.20	78.84	18.70	14.16	1.62
2003/04	9245.90	77.62	19.19	14.83	1.72
2004/05	10159.40	77.72	18.77	14.48	1.73
2005/06	10373.70	74.27	18.00	14.35	1.58
2006/07	15034	79.20	21.13	14.14	2.07
2007/08	17311.22	74.98	20.32	16.08	2.11
2008/09	21418.05	72.42	20.97	16.95	2.55
Total	100412.20	-	-	-	-
Average	12551.52	77.38	19.96	15.33	1.92

Source: Economic survey July, 2009

Above Table 4.8 shows that the income tax was increased almost three times more then the FY 2001/02, in FY 2008/09. In FY 2001/02 it was Rs 8903.70 million and it increased to Rs 21418.05 million in FY 2008/09. But the percentage contribution of income to total tax revenue was decreased. In FY 2001/02 it is 84.01 percent which decreased to 72.42 percent in FY 2008/09. The contribution of income tax to total tax revenue was 22.63 percent in FY 2001/02 which was decreased to 20.97 percent in FY 2008/09. Similarly its contribution to total revenue was 17.65 percent in FY 2001/02 and decreased to 16.95 percent in FY 2008/09. The contribution of income tax to GDP was 1.94 percent in FY 2001/02 which was increased to 2.55 percent in FY 2008/09. the average percentage contribution of income tax to total direct tax, total tax revenue, total revenue and GDP were 77.38 percent, 19.96 percent, 15.33 percent and 1.92 percent respectively during the study period of eight years.

From the Table 4.7, it can be said that the income tax is the major component of direct tax in Nepal. But the contribution of income tax to total tax revenue is still lower as compare to other developing countries and also the contribution of income tax to total revenue and GDP are not satisfactory in Nepal.

4.1.8 Composition and trend of income tax.

In earlier 1993/94 income tax revenue was divided into three categories i.e. corporate income tax, individual income tax and remuneration. After the FY 1993/94, income tax was divided into four categories, they were corporate income tax, individual income tax, house and land rent tax and interest tax. Corporate income tax is collected from public corporation, Semi-public Corporation and private corporate bodies and partnership firms. Individual income tax is collected from industry, business, profession and vocation and remuneration. Interest tax is collected from banks and financial institution that pay interest on all types of deposits and the urban house and land rent tax is levied on income derived from renting the house and land in urban areas. The following table shows the composition and trend of the income tax revenue:

Table 4.8 Components of income tax and trends in different years

(Rs in million)

Years / Sources of income tax	2001/02	2002/03	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09
A. Corporate income tax	3181.34	2487.29	3587.90	3800.20	3600.00	6736.80	7391.04	8316.45
i. public enterprises	1769.33	1251.02	2056.60	1332.40	195.70	1019.70	204.58	722.10
ii.Semi-Public enterprises	00	00	00	00	00	00	00	00
iii. Private corporate bodies	142.01	1236.27	1531.30	2467.80	3404.30	5717.10	7186.46	7594.35
B. Individual income tax	4419.09	3362.20	3533.40	3926.30	4234.70	5234.40	6381.21	8608.65
i. Remuneration	835.56	1252.20	1391.20	1675.90	1764.10	2007.40	2451.04	2709.6
ii. Industry, business, profession, and others	3583.53	2110	2142.20	2250.40	2470.60	3227.00	3930.17	5899.05
C. Urban house and land rent tax	2.29	00	00	00	00	00	00	00
D. Interest tax	467.70	864.00	733.40	757.00	774.90	1054.90	1087.23	1783.35
Total	8903.70	7966.20	9245.90	10159.4	10373.7	15034	17311.22	21418
% increase of income tax collection	-	10.53	16.06	9.88	2.10	45.87	15.14	23.72

Source: Economic survey July, 2009

Above Table 4.9 shows that the amount of corporate income tax was in increasing trend till the FY 2004/05 amounting to Rs 3800.20 million and in FY 2005/06 it decreased to 3600.00 million. After that from FY 2006/07 it started to increase and reached to Rs 8236.41 million in FY 2008/09. The amount of individual income tax was 4419.09 million in FY 2001/02 and it decreased to Rs 3362.20 million in FY 2002/03. After that it was in increasing trend. In FY 2003/04 it is 3533.40 million and increased to Rs 8608.65 million in FY 2008/09. The income tax from industry, business, profession and vocation and others was higher than the income tax from remuneration in income tax.

The contribution of interest tax to total income tax was Rs 467.70 million in FY 2001/02 which increased to Rs 864.00 million in FY 2002/03. In FY 2003/04 it decreased to Rs 733.40 million. After that it was in increasing trend and reached to 1783.35 million in FY 2008/09.

The percentage increased in income tax collection is 10.53 percent in FY 2002/03. It was in fluctuating trend. It was minimum, in FY 2005/06 i.e. 2.10 percent and maximum in FY 2006/07 i.e. 45.87 percent it was the highest increment during the study period of eight years.

4.1.9 Composition of income tax

Income tax is composed of from corporate income tax, urban house and land rent tax, individual income tax, remuneration and interest tax. Corporate income tax is collected from public enterprises, semi- public enterprises, private corporate bodies and partnership firms. Individual income tax is collected from industry, business and profession or vocation. Remuneration tax is collected from the employee. Interest tax is collected from banks and financial institutions that pay interest on all types of deposits. The composition of income tax is shown in the following table:

Table 4.9 Composition of income tax

(Rs in million)

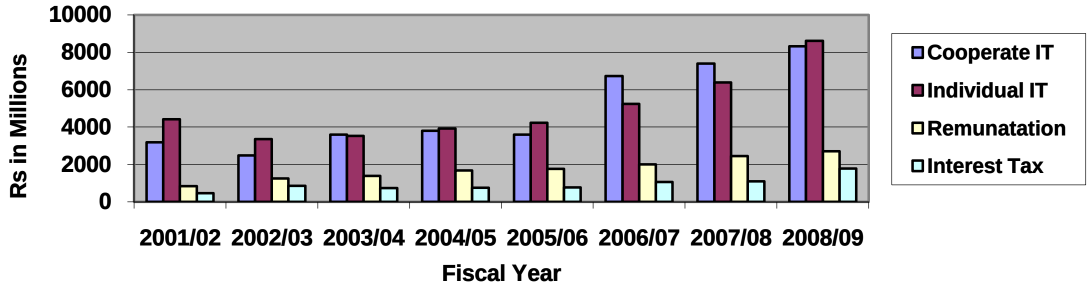
Fiscal year	Total IT	Corporate IT	% of IT	Individual IT	% of IT	Remune-ration	% of IT	Interest tax	% of IT
2001/02	8903.70	3181.30	35.73	4419.09	49.63	835.56	9.39	467.70	5.25
2002/03	7966.20	2487.30	31.22	3362.20	42.20	1252.60	15.74	864.00	10.8
2003/04	9245.90	3587.90	38.80	3533.40	38.22	1391.20	15.05	733.40	7.93
2004/05	10159.40	3800.20	37.40	3926.30	38.65	1675.90	16.50	757.00	7.45
2005/06	10373.70	3600.00	34.70	4234.70	40.82	1764.10	17.01	774.90	7.47
2006/07	15034.00	6736.80	44.81	5234.40	34.18	2007.90	14.00	1054.9	7.01
2007/08	17311.22	7391.04	42.69	6381.21	36.86	2451.04	14.17	1087.9	6.28
2008/09	21418.05	8316.45	38.82	8608.65	40.19	2709.60	12.67	1783.3	8.32
Total	100412.2	39100.99		39699.9		14087.9		7523.1	
Average	12551.52	4887.63	38.02	4962.48	40.09	1760.98	14.33	940.38	7.56

Source: Economic survey July, 2009

Above Table 4.9 shows that the contribution of corporate income tax to total income tax was 35.73 percent in FY 2001/02 amounting to Rs 3181.30 million. It was decreased to 31.22 percent in FY 2003/04. It was in fluctuating trend during the study period an in FY 2008/09 the contribution of corporate income tax to total income tax was 38.82 percent. But the amount of corporate income tax was in increasing trend except the FY 2002/03 i.e. in FY 2001/02 it is 3181.30 million and increased to 8316.45 million in FY 2008/09. The contribution of individual income tax to total income tax was also in fluctuating trend it was 49.63 percent in FY 2001/02 and decreased to 42.2 percent in FY 2002/03 and it further decreased to 38.22 percent in FY 2003/04 after that it slightly increased to 40.82 percent in FY 2005/06. The contribution of individual income tax to total income tax in FY 2008/09 was 40.19 percent amounting to Rs 8608.65 million. The contribution of remuneration to total income tax was 9.39 percent in FY 2001/02. It increased to 16.50 percent in FY 2004/05. Its maximum contribution to total income tax is in FY 2005/06 i.e. 17.01 percent amounting to Rs 1764.10 million. In FY 2008/09 the contribution of remuneration to total income tax was 12.67 percent. The contribution of interest tax to total income tax was 5.25 percent in FY 2001/02 it increased to 10.84 percent in FY 2002/03 after that it started to decreased and come down to 6.28 percent in FY 2007/08. In FY 2008/09 its contribution was increased to 8.32 percent. The average contribution of corporate income tax, individual income tax, remuneration and interest tax were 38.02 percent, 40.09 percent, 14.33 percent and 7.56 percent respectively during the study period of eight years.

The following figure shows the composition of income tax:

Figure 4.6 Composition of income tax



4.1.10 Exemption Limit in Nepalese Income Tax Act.

Exemption limit system for calculating the taxable income and tax liability was introduced, when the Act was introduced. Till the FY 1966/67, exemption limit allowed as same amount for all kinds of taxpayers. But from the FY 1967/68, exemption limit allowed as differently for different types of taxpayers. Now days it is allowed only to personal income i.e. for natural person and sole proprietor business.

Generally, the government has raised the exemption limit every year. It was Rs 7000 thousand for all taxpayer in the FY 1959/60. it was gradually decreased to Rs 6000 thousand and Rs 5000 thousand for FY 1963/64 to 1964/65 and 1965/66 to 1966/67 respectively. After the FY 1967/68, the exemption limit was allowed only for individual, couple and family separately and from the FY 1979/80, the couple and family are provided for the income tax exemption limit equally. After the implementation of income tax Act 2002, the word 'family' has been removed for the purpose of exemption limit. Just announced budget speech for the FY 2009/10 allowed Rs 1600000 for individual and Rs 200000 for couple as exemption limit. The following table shows the exemption limit provided in the various years.

Table 4.10 Exemption limit in the Nepalese income tax (For the fiscal year 1979/80 to 2008/09)

Fiscal year	Individual	Couple	Family
1979/80-1980/81	7500	10000	10000
1981/82-1982/83	10000	15000	15000
1983/84-1989/90	15000	20000	20000
1990/91-1991/92	20000	30000	30000
1992/93-1996/97	25000	35000	35000
1997/98	30000	40000	40000
1998/99	40000	50000	50000
1999/2000	50000	60000	60000
2000/01-2001/02	55000	75000	75000
2002/03	65000	85000	-
2003/04	65000	85000	-
2004/05	80000	100000	-
2005/06	85000	115000	-
2006/07	100000	125000	-
2007/08	115000	140000	-
2008/09	125000	140000	-
2009/10	160000	200000	-

Source budget speech of various years, GON, MOF

4.1.11 Income Tax Rate

Tax rate and its structure have been changing frequently since its introduction in 1959/60. Since 1959/60 to date, there are various records of highest and lowest income tax rate. In 1963/64, the lowest income tax rate was 4 percent and in 1975/76, the highest income tax rate was 60 percent. After introducing of income tax, tax rate is charged on different slabs. In 1975/76, the income tax rate for personal income was 10 percent to 60 percent for 7 different slabs. Form 1998/99 to till date, the income tax rate for personal income is 15 percent and 25 percent for two different slabs.

Under new Income Tax Act 2001; individual income tax is levied with two rates of 15 percent and 25 percent. For individuals; who have Rs. 120,000 income or Rs. 1200,000 turnover form any kind of business in metropolitan or sub-metropolitan cities, municipalities and other areas in Nepal are subject to pay tax as follows:

Metropolitan or sub-metropolitan cities	Rs. 2000
Municipalities	Rs. 1500
Anywhere else in Nepal	Rs. 1000

The income tax rate for partnership firms, corporations and non-resident was 15 to 60 percent for different slabs in 1975/76 which decreased to 30 and 25 percent for total taxable income. Income tax act has provided rebates or facilities so only 20 percent is taxed on their income for a special industry.

Different sets of tax rates are levied for different slabs. The following table shows the rates for personal income tax in Nepal.

Table 4.11 Rates of personal incomes tax in Nepal (2001/02 to 2008/09) (Figure in Rs. Thousand)

Fiscal Year	Slabs over exemption limit		
	1	2	3
2001/02	First Rs 75000 15%	Balance 25%	Additional 1.5%
2002/03	First Rs 75000 15%	Balance 25%	"
2003/04	First Rs75000 15%	Balance 25%	"
2004/05	First Rs 75000 15%	Balance 25%	"
2005/06	First Rs 75000 15%	Balance 25%	"
2006/07	First Rs 75000 15%	Balance 25%	"
2007/08	First Rs 85000 15%	Balance 25%	-
2008/09	First Rs 85000 15%	Balance 25%	-

Sources: finance Act of various years, MOF, GON

From the above Table 4.11, it can be seen that the rate of personal income tax in Nepal for last eight years had been not changed significantly, from FY 2001/02 to 2006/07 there was 15 percent tax rate for first Rs 75000 and 25 percent for the balance and additional 1.5 percent for balance too. From the FY 2007/08 to 2008/09 there was 15 percent for first Rs 85000 and 25 percent for balance and the additional tax for balance had been eliminated.

Similarly, income tax rate was charged for partnership firms, corporation and non-residents. The exemption limit for them is not provided by the income tax Act. Tax is charged on the income after deducting all expenses. The income tax rates approved for different years are given below:

Table 4.12 Income tax rates for partnerships firms, corporation and non-residents (2001/02 to 2008/09)

Fiscal Year	A	B	C
2001/02	30%	25%	20%
2002/03	30%	25%	20%
2003/04	30%	25%	20%
2004/05	30%	25%	20%
2005/06	30%	25%	20%
2006/07	30%	25%	20%
2007/08	30%	25%	20%
2008/09	30%	25%	20%

Source: finance Acts of various years, MOF, GON

Where ,

(A) Income tax rate for banks and financial companies and alcohol/tobacco industry.

(B) Income tax rate for others (including partnership firms)

(C) Income tax rate for special industry.

The above Table shows that the income tax rates for partnership firms, corporation and non-resident were different for different form of the business character. From 2001/02, to till date, the tax rates are 30 percent for banking and financial institutions and tobacco and alcohol industries, 25 percent for other (including partnership firms) and 20 percent for the special industry at a flat rate on taxable income.

4.2 An Empirical Analysis

4.2.1 Introduction

An empirical investigation has been conducted in order to find out various aspects of income tax from the experience of the real world. The major tools used for this purpose is an opinion questionnaire, which was dispatched to 75 persons representing tax administration, tax experts and taxpayers, but only 50 responses were received. The questionnaire (Appendix I) included the various aspects of income tax concerning with provisions of exemptions and deductions and contribution of income tax to the government revenue. The questionnaire either asked for a Yes/No response or asked for ranking of choice according to number of alternatives where a first choice was most important and last choice was least important. Information received from respondents were tabulated into the separate format and they were expressed in percent of total numbers or points then analyzed into descriptive way.

The following table shows the groups of respondents and code used to represent them,

Table 4.13 Groups of respondents and code used

S.N.	Groups of respondents	Sample size	Code used
1	Tax experts	10	A
2	Tax administrators	20	B
3	Taxpayers	20	C
Total		50	

Source: as organized by the researcher

4.2.2 Contribution of Income Tax to National Revenue of Nepal

In order to know the respondent's opinion about the contribution of income tax to national revenue of Nepal, a question was asked, "Do you think that contribution of income tax to national revenue of Nepal is satisfactory? The responses were received from the respondents which are tabulated as follows:

Table 4.14 Contribution of income tax to national revenue of Nepal

S.N	Responses Respondents	Yes		No		Total	
		No.	%	No.	%	No.	%
1	A	4	40	6	60	10	100
2	B	8	40	12	60	20	100
3	C	9	45	11	55	20	100
Total		21	42	29	58	50	100

Source: opinion survey, 2010.

From the Table 4.14, it was found that only 40 percent of tax experts, 40 percent of tax administrators and 40 percent of tax experts were believed that the contribution of income tax to national revenue is satisfactory and rest 60 percent of tax experts, 60 percent of tax administrator and 55 percent of tax payers reacts adversely. In total 42 percent of the respondents were believed that the contribution of income tax to national revenue is satisfactory and 58 percent of the respondents were against it.

4.2.3 Soundness and Effectiveness of income tax administration in Nepal.

In order to know the respondent's opinion about the soundness and effectiveness of income tax administration, a question was asked with the respondents, "Do you think that the income tax administration of Nepal is sound and effective?" The responses received from the respondents are tabulated as follows:

Table 4.15 Soundness and effectiveness of income tax administration of Nepal

S. N	Responses Respondents	Yes		No		Total	
		No.	%	No.	%	No.	%
1	A	3	30	7	70	10	100
2	B	12	60	8	40	20	100
3	C	6	30	14	70	20	100
Total		21	42	29	58	50	100

Source: Opinion survey, 2010.

From the opinion survey, it was found that 30 percent of tax experts, 60 percent of tax administrators and 30 percent of tax payer believed that the income tax administration of Nepal is sound and efficient where as majority of tax experts and tax payer i.e. 70

percent of tax experts and 70 percent of tax payer were disagreed about it. In total 58 percent of the respondents believed that the income tax administration of Nepal is not sound and efficient. But the majority of tax administrators were against it.

4.2.4 Major causes, which are responsible for the unsound and ineffective income tax administration of Nepal.

58 percent of the respondents believed that the income tax administration is not sound and efficient. Therefore, to know the major causes of it, a question was asked, which are responsible for the creation of unsound and ineffective income tax administration of Nepal? The respondents are requested to rank among nine options as per their priority. The ranking results are tabulated as follows.

Table 4.16 Major causes, which are responsible for the unsound and ineffective income tax administration of Nepal

S.N.	Major causes	Group			Total frequency	Percentage	Ranking
		A	B	C			
a	Defective assessment procedure	40	82	90	212	12.47	7
b	Lack of public participation	25	48	60*	133	7.82	2
c	Lack of tax education	25	70	75	170	10.0	4
d	Lack of trained and competent employees	35	60	85	180	10.58	5
e	In efficient tax administration	55	86	114	253	15.0	8
f	Weakness in government's economic policy	25	40*	65	130	7.64	1
g	Inefficient organizational structure of tax administration	53	89	120	262	15.42	9
h	Complicated tax laws and provisions	23*	60	70	153	9.0	3
I	Corruption	45	90	70	205	12.07	6
Total		326	625	749	1700	100	-

Source: opinion survey, 2010.

From the Table 4.16, rank 1 is given to the lowest percentage and 9 to the highest. Here lowest percentage is obtained by the causes, which is treated as the most important causes by the respondents.

From the above Table 4.16, the major causes of unsound and inefficient of income tax administrations are ranked in order of reference of the respondents are as follows:

1. Weakness in government's economic policy.
2. Lack of public participation.
3. Complicated tax laws and provisions.
4. Lack of tax education.
5. Lack of trained and competent employees.
6. Corruption.
7. Defective assessment procedure.
8. Inefficient tax administration.
9. In efficient organizational structure of tax administration.

The table 4.16 shows that, tax experts believed that the major causes of being unsound and ineffective income tax administration of Nepal was "complicated tax laws and provisions". Where as tax administrators and tax payers believed that the major causes were "weakness in government economic policy" and "lack of public participation" respectively.

4.2.5 Opinion on the Current Income Tax Rate.

In order to know the opinion on the current income tax rate respondents were requested to tick only among the three alternatives (High, Medium and Low) the question asked was, "what is your opinion about the current income tax rate ?" the responses received were tabulated as follows.

Table 4.17 Opinion on the current income tax rate

S.N	Responses Respondents	High		Medium		Low		Total	
		No.	%	No.	%	No.	%	No.	%
1	A	3	30	5	50	2	20	10	100
2	B	5	25	13	65	2	10	20	100
3	C	9	45	11	55	-	-	20	100
		17	46	29	58	4	8	50	100

Source: opinion survey, 2010.

From the above opinion survey, 30 percent of tax experts, 25 percent of tax administrators and 45 percent of tax payers were believed that the current income tax rate is high. On the other hand, 50 percent of tax experts, 65 percent of tax administrator and 55 percent of tax payers were believed that the current income tax rate is medium. Where as 20 percent of tax experts and 10 percent of tax administrator were believed that the current income tax rate is low. In total, 58 percent of respondents were agreed that the current income tax rate is medium. Where as 34 percent of respondents agreed that the current income tax rate is high and rest 8 percent believed that the current income tax rate is low. From the table it can be concluded that the current income tax rate is medium.

4.2.6 Sufficiency of Exempted Items of Income Tax.

Income tax Act 2002 has provided exemption to the various incomes. To know the opinion of the respondents about the sufficiency of exempted items of income, a question was asked, "Do you think that the exempted items of income are sufficient?" the responses were as follows.

Table 4.18 Sufficiency of exempted items of income

S.N	Responses Respondents	Yes		No		Total	
		No.	%	No.	%	No.	%
1	A	4	40	6	60	10	100
2	B	15	75	5	25	20	100
3	C	8	40	12	60	20	100
Total		27	54	23	46	50	100

Source: opinion survey, 2010.

From the Table 4.18, 40 percent of tax experts, 75 percent of tax administrator and 40 percent of tax payer were thought that exempted items of income tax are sufficient. Where as 60 percent of tax experts, 25 percent of tax administrators and 60 percent of tax payers thought that exempted items of income tax are not sufficient. In total 54 percent respondents are believed that the exempted items of income tax are sufficient and rests of respondents are against it.

As who gave the negative response about the sufficiency of exempted items of incomes were asked another question "if no, "what kind of income should be exempted?" they were requested to write their opinion. Most of the respondents did not response about it. Only few responses were received which are as follows:

A Tax experts

- Income from interest and rent.
- Income derived by tax exempted organization.
- Income from provident fund (capital gain).
- Income from life insurance.
- Awards and rewards.
- Rational exemption should be given to all kind of incomes.

B tax administrators.

- Medical allowance.
- Retirement benefits.

C Tax payers.

- Medical allowance.
- Overtime allowance.
- Remote area allowance.
- Income from life insurance.
- Educational allowance for children.
- Medical expenses on the basis of bills.

4.2.7 Adequateness of Current Income Tax Exemption Limit.

Finance Acts of Nepal yearly prescribes the tax rate and exemption limit of income. Exemption limit and tax rate are introduced when the income tax was introduced. It is changing yearly from the beginning of its introduction. To know the opinion of the respondents about the current exemption limit, a question was asked, "Do you think that the current income tax exemption limit is adequate?" The responses of the respondents are as follows.

Table 4.19 Adequateness of current income tax exemption limit

S.N	Responses Respondents	Yes		No		Total	
		No.	%	No.	%	No.	%
1	A	4	40	6	60	10	100
2	B	7	35	12	65	20	100
3	C	5	25	15	75	20	100
Total		16	32	34	68	50	100

Source: opinion survey, 2010.

Above Table 4.19 shows that 40 percent of tax experts, 35 percent of tax administrators and 25 percent of tax payers believed that the current exemption limit of income is adequate. Where as 60 percent of tax experts 65 percent of tax administrator and 75 percent of tax payers were believed that the current exemption limit of income is inadequate. In total 68 percent of respondents respondent were thought that current exemption limit of income is inadequate where as 34 percent were against it. From the opinion of the respondents it can be concluded that the current exemption limit of income is inadequate. The respondents who were against the current exemption limit were asked a question, if no, "which of these exemption limit do you suggest for an individual and a couple or a family?" the responses of respondents were tabulated as follows.

Table 4.20 Suggestion of exemption limit for an individual

Respondents Responses	Group			Total number	%	Ranking
	A	B	C			
Rs. 190,000	-	2	2	4	12	3
Rs. 200,000	2	4	5	11	32	2
Rs. 220,000	4	7	8	19	56	1
Total	6	13	15	34	100	-

Source: opinion survey, 2010.

From the Table 4.20 it can be seen responses about the exemption limit of an individual, it was found that 56 percent of the respondents in favors of Rs 220,000 where as 32 percent of the respondents suggested that the exemption limit should be Rs 200,000 and 12 percent of respondents suggest to Rs 190,000.

Table 4.21 Suggestion of exemption limit for a couple or a family

Respondents / Responses	Group			Total number	%	Ranking
	A	B	C			
Rs. 230,000	1	1	2	4	11	4
Rs. 245,000	-	2	3	5	14	3
Rs. 260,000	2	4	4	10	29	2
Rs. 275,000	3	6	6	15	46	1
Total	6	13	15	34	100	-

Source: opinion survey, 2010.

From the above Table 4.21, it is clear that most of the respondents (i.e. 46%) suggested for Rs. 275,000 as exemption limit for a family. 29 percent of the respondents suggested for Rs. 260,000 also Rs. 245,000 and Rs. 230,000 suggested by respondents of 14% and 11% respectively. It can be concluded that most of the respondents are in favour of Rs. 275,000 as an exemption limit for a couple or a family. On the personal discussion with the respondents, the researcher found that more people were in support to provide income tax exemption limit equivalent to annual remuneration income of a government employed section offices.

4.2.8 Family Exemption Limit According to the Number of Dependents

Income tax act has provided exemption limit to a family. But it has not defined the number of dependents within a family. So, to know the opinion about the exemption limit of a family according to the number of respondents, a question was asked, "Do you agree that family exemption limit must be provided according to the number of dependent?" The responses were as follows:

Table 4.22 Family exemption limit on the basis of the number of dependents

S.N	Responses / Respondents	Yes		No		Total	
		No.	%	No.	%	No.	%
1	A	2	20	8	80	10	100
2	B	6	30	14	70	20	100
3	C	12	60	8	40	20	100
Total		20	40	30	60	50	100

Source: opinion survey, 2010.

The above Table 4.22 shows the response of respondents about the family exemption limit that must be provided according to the number of dependents. Out of the 100 percent response, 60 percent of the respondents disagreed whereas 40 percent of the respondents agreed that the family exemption limit must be provided according to the number of dependents. The majority of respondents of tax experts and tax administrators were disagreed but the tax payers were agreed on providing the family exemption limit according to the number of dependents.

On the personal discussion, either of any group of the respondents having micro family was against on providing the family exemption limit according to the number of dependents due to their lowest exemption limit. But as a whole, it can be concluded that most of the respondents disagreed on providing the family exemption limit according to the number of dependents., Researcher also found that respondents were in favour to provide exemption limit to a family according to the number of dependents but it is difficult to execute because it is impossible to apply in real field.

Similarly, another question was asked to know the opinion of respondents or exemption limit that should be adjusted according to the inflationary situation of the country. The question was, "Do you agree that exemption limit should be adjusted according to the inflationary situation of the country?" The responses were:

Table 4.23 Exemption limit according to the inflationary situation of the country

S.N	Responses / Respondents	Yes		No		Total	
		No.	%	No.	%	No.	%
1	A	4	40	6	60	10	100
2	B	14	70	6	30	20	100
3	C	16	80	4	20	20	100
Total		34	68	16	32	50	100

Source: opinion survey, 2010.

The above Table 4.23 shows that, the majority of tax administrators and tax payers were agreed to adjust the exemption limit according to the inflationary situation of the country where as tax experts were against it. In total 68 percent of respondents were thought that the exemption limit should be adjusted according to the inflationary situation of the country but 32 percent were disagreed about it. Therefore it can be concluded that the exemption limit of a family or a couple or an individual should be adjusted according to the inflationary situation of the country.

4.2.9 Opinion on Providing Exemption Limit on Agriculture Income

After commencing of Income Tax Act, agricultural income has been treated as taxable income in sometimes in a specific case and sometime as exempted income too. The new Income Tax Act has exempted agricultural income tax other than the income from company, or partnership, or corporate body, or through the land above the holding ceiling an prescribed in land act 2001. To know the opinion on it one question was asked as, "What is your opinion on exemption providing on agricultural income?" The following table shows the responses of respondents;

Table 4.24 Exemption on agricultural income

Respondents / Responses	Group			Total number	%	Ranking
	A	B	C			
Yes, it should be exempted	6	11	15	32	64	1
No, it shouldn't be exempted	2	4	-	6	12	2
It should be treated as other income	2	3	3	8	16	3
Other, (if any, specify)	-	2	2	4	8	4
Total	10	20	20	50	100	-

Source: opinion survey, 2010.

Above Table 4.24, shows 64 percent of the total respondents were in support to exempt the agricultural income whereas 12% of the respondents were against the exemption of agricultural income. Only 16% of the respondents were in favour to treat it as other income. The respondents who specified their responses as other incomes were given the following suggestions;

- Commercial agricultural income should be taxed as other income
- A separate, agricultural income tax Act should be presented.
- A practical arrangement for taxing agriculture should be formulated, for example, base on the size of landholding.
- Organizational agricultural income should be given exemption for limited period of establishment.

4.2.10 Sufficiency about the Itemized Deductions

Income Tax Act 2002 has provided different kinds of expenses as deductions. Some expenses are allowed for deduction as itemized deduction and some are standard deduction.

In order to know the attitude towards the item-wise deduction of expenses, a question was asked as, "Do you think that the itemized deductions are sufficient?" The responses were as follows:

Table4.25 Sufficiency about itemized deductions

S.N	Responses Respondents	Yes		No		Total	
		No.	%	No.	%	No.	%
1	A	4	40	6	60	10	100
2	B	12	60	8	40	20	100
3	C	8	40	12	60	20	100
Total		34	48	26	52	50	100

Source: opinion survey, 2010.

The Table 4.25 shows that the majority of the respondents were believed that the itemized deduction provided by the income tax Act is insufficient except tax administrators, majority of tax experts and tax payers i.e. 60 percent of tax experts and 60 percent of tax payers believed that itemized deduction of the expenses are not sufficient. But 60 percent of tax administrators were believed that the itemized deduction is sufficient.

From the table 4.25 it can be concluded that there are insufficiencies about the itemized deductions of expenses.

The respondents who were against it, another question was asked “if no, “what kind of other expenses should be deducted while computing taxable income?” the respondents requested to write in the blank orders. Few respondents replied responses which are classified according to the code used in number-wise.

A. Tax experts

- Repair and maintenance should be fully allowed there is no meaning of allowing only 7% of the depreciation base according to the existing provision.
- Special Economic Zones (SEZ) should be created and alternative tax administration, exemption allowed for industries, processing units; infrastructure development projects in such regions.

B. Tax Administrators

- Daily T.A. expenses from residence to business.
- Educational expenses.
- Traveling expenses.
- Delivery expenses.

C. Taxpayers

- House rent
- Educational allowance
- Medical expenses on the basis of bills.
- Tiffin allowance.
- Traveling allowance.

4.2.11 Opinion on Providing Additional Exemption to an Individual Working in Different Remote Areas

Income tax Act 2002 has provided the additional exemption of Rs 30000, Rs 24000, Rs18000, Rs 12000, Rs 6000 to an individual who is working in the different remote areas i.e. remote areas A,B, C, D, and E. to know the opinion of the respondents about additional exemption which is given to an individual. Who are working in different remote areas of the country is suitable or not, a question was asked, in your opinion, "is it suitable that the additional exemption given to an individual who is working in the different remote areas?" the responses of the respondents are tabulated as follows.

Table 4.26 Opinion on providing additional exemption to an individual working in different remote areas

S.N	Responses / Respondents	Yes		No		No Responses		Total	
		No	%	No	%	No	%	No	%
1	A	5	50	5	50	-	-	10	100
2	B	16	80	2	10	2	10	20	100
3	C	12	60	4	20	4	20	20	100
Total		33	66	11	22	6	12	50	100

Source: opinion survey, 2010.

From the Table, 50 percent of tax experts, 80 percent of tax administrator and 60 percent of tax payers were agreed that the additional exemption to an individual who are working in the different remote areas in the country is sufficient Where as 50 percent of tax experts, 10 percent of tax administrators and 20 percent of tax payers were disagreed with the current additional exemption facility. And other 10 percent of tax administrators and 20 percent of tax payers were did not provide any responses about it. In total 66 percent of the respondents were agreed that the current additional exemption to an individual who is working on different remote areas is suitable. 22 percent of respondents disagreed with the current exemption facility and rest 12 percent of respondents did not provide any responses. From the table majority of respondents were agreed with the current additional exemption for an individual who is working in the different remote area is suitable or proper.

On the personal discussion with the respondents it was found that according to the economic condition and per capita income of the country current additional tax exemption to the individual working in the different remote area is suitable or proper.

4.2.12 Additional Tax Exemption Facility to the Special Industries Established in Different Areas

Income tax Act 2002 has provided additional exemption facilities for 10 income years to the special industries established in different areas i.e. industries established in remote areas, undeveloped areas and underdeveloped areas have to pay 70 percent, 75 percent and 80 percent of applicable tax rate respectively up to ten income years commencing from and including the year in which the operation commences. To know the opinion of the respondents about such facility, a question was asked; “Is it suitable to provide additional facilities to the special industries established in the different areas in the country?” the responses of the respondents were as follows.

Table 4.27 Additional tax exemption facilities to special industries established in different areas

S.N	Responses Respondents	Yes		No		No Responses		Total	
		No.	%	No.	%	No.	%	No.	%
1	A	6	60	2	20	2	20	10	100
2	B	12	60	5	25	3	15	20	100
3	C	13	65	5	25	2	10	20	100
Total		31	62	12	24	4	14	50	100

Source: opinion survey, 2010.

From the Table 4.27, it can be said that 62 percent of respondents agreed with the current additional facilities to the special industries established in the different areas whereas 24 percent of respondents were disagreed with the current additional tax exemption facilities to the industries established in the different areas. And 14 percent respondents did not provide any responses about the question. Majority of tax experts, tax administrators and tax payers were agreed with the present exemption facility. So it can be concluded that the current facility is proper or suitable.

Similarly, another question was asked to the respondents who disagreed with the present additional exemption facility provided by income tax Act 2002 to the special industries established in the different areas. The question was, “how much additional tax exemption should be provided?” the responses given by the respondents are as follows.

The respondents suggested that the facility should be given for the long period of time to attract the industry in such areas.

Respondents suggested that the special industries established in remote area, undeveloped area and underdeveloped area should pay tax 40 percent, 50 percent and 75 percent of applicable tax rate respectively for ten income years.

4.2.13 Problems and Weakness of Nepalese Income Tax System

Income tax system of Nepal has been blamed that it is not efficient. To know the opinion of the respondents about the causes of problems and weakness of Nepalese income tax system, a question was asked, “What are the major problems and weakness in the Nepalese income tax system?” the respondents were requested to rank the given causes from 1 to 10. The results of the opinion survey is presented in the following table.

Table 4.28 Problems and weakness of nepalese income tax system

S.N	Problems and weakness	Respondents			Total frequency	%	Rank
		A	B	C			
1	Lack of tax education	7	14	9	30	12.10	7
2	Relatively high tax rate	5	10	7	22	8.87	4
3	Difficult to maintain the account for tax purpose	3	7	5	15	6.05	2
4	Limited tax base	7	15	3	25	10.08	6
5	Lack of corporation	9	11	14	34	13.71	9
6	Lack of clear provision under income tax law	2	5	4	11	4.43	1
7	Ambiguous provision in income tax law	6	10	8	24	9.68	5
8	Lack of trained employee	8	17	12	37	14.92	10
9	Lack of timely adjustment of tax law	5	7	7	19	7.66	3
10	Increased corruption	7	15	9	31	12.50	8
Total					248	100	

Source: opinion survey, 2010.

From the above Table 4.28, according to the preference of the respondents major problems and weakness of the Nepalese income tax system are ranked as follows:

1. Lack of clear provision under the income tax law.
2. Difficult to maintain the account for tax purpose.
3. Lack of timely adjustment of tax law.
4. Relatively high tax rate.
5. Ambiguous provision in income tax law.
6. Limited tax base.
7. Lack of tax education.
8. Increased corruption.
9. Lack of corporation.
10. Lack of trained employees.

From the above Table 4.28, it can be concluded that the major problems and weakness of Nepalese income tax system are lack of clear provision in the income tax law, difficult to maintain account for tax purpose, increase corruption, lack of trained employees in tax administration and lack of corporation among tax administrators and tax payers.

On the personal discussion with the respondents, the researcher found that increased corruption is major problem and weakness of Nepalese income tax system.

4.2.14 Sufficiency of Provision Relating to Exemptions and Deductions.

In order to know the sufficiency of provisions relating to exemptions and deductions under the Nepalese Income Tax Act, respondents were requested to give their response in yes/no alternatives. The question was asked as, "In your opinion, are the provisions relating to exemptions and deductions under the Nepalese Income Tax Act sufficient in all aspects?" The responses received on it are tabulated as below:

Table 4.29 Sufficiency of provisions relating to exemptions and deduction under the nepalese income tax act

S.N	Responses Respondents	Yes		No		Total	
		No.	%	No.	%	No.	%
1	A	4	40	6	60	10	100
2	B	14	70	6	30	20	100
3	C	5	25	15	75	20	100
Total		23	46	27	54	50	100

Source: opinion survey, 2010.

From the Table 4.29, it is seen that 40 percent of tax experts, 70 percent of tax administrators and 25 percent of tax payers believed that the provision relating to exemptions and deductions under the Nepalese income tax Act is sufficient whereas

60 percent of tax experts, 30 percent of tax administrators and 75 percent of tax payers were against it. In total 46 percent of respondents were agreed whereas 54 percent of respondents were disagreed about the sufficiency of provision relating to exemptions and deductions under the Nepalese income tax Act 2002. From the table, it can be concluded that majority of respondents were against the sufficiency.

The respondents who gave the negative responses about the sufficiency of provision relating to exemptions and deductions under the Nepalese income tax Act another question was asked and requested to give their responses on blank order. The question was, “if no, “which aspects the improvements are needed?” the responses received from the respondents for the improvements of different aspects of Nepalese income tax Act are as follows.

A Tax Experts

- Tax administration.
- Income tax administration.
- Attitude of tax administrators.
- Tax base should be widen.
- Payments system.
- Monitoring system.
- Exemption limit.
- Under multiple rate system.

B Tax Administrators

- Accounting system.
- Functional system.
- Simplify the language.
- Remove complicated provisions.
- Specification of the job of the department.
- Computerized system in all tax offices.

C Tax Payers

- Remuneration income.
- Language.
- Depreciation system.
- Tax administration.
- District wise tax offices.
- Exemption limit on the basis of inflation.

- Tax on property.

From the above aspects for improvements, most of the respondents were suggested to improve tax law and language to be simplified. They also focused to improve the tax administration too.

4.2.15 Suggestions about Income Tax in Nepal

Income Tax Act 2002 is better than earlier Income Tax Act 1974, but this new act is not free from weaknesses and vague and complicated language used. Thus a question was asked to give suggestions about income tax in Nepal. The question was asked as, "Do you have any suggestions about income tax in Nepal?" Only few respondents of all kinds of group have given the suggestions which are given below;

- The tax laws needs to be simplified, easily interpreted and understood by even a layman.
- Tax administration and assessment procedures are also required to be simplified and should be made taxpayers as friendly..
- Accessibility of the tax administration should be improved.
- Utilization of revenue takes vital role to revenue generation and voluntarily self registration and assessment.
- Public awareness is needed and political commitment and credibility should be necessary.
- Income tax act should facilitate people to pay tax by making honestly and friendly organization and employees.
- It should give focus on the area of taxation rather than high tax rate.
- Lowering tax rate and increasing tax base
- Increasing exemption limit.
- Motivating for self-compliance.
- Developing competence within tax personnel.
- Starting court cases to evading people/entity.
- Compulsory declaration of assets of each individual.
- Different privilege and nation-wise recognition must be given to the regular and high taxpayers and also should give for abroad visiting.
- Punishment should be given for not paying tax to the government.

4.3 Heads of Income and Exemption and Deduction Provided by Income Tax Act 2002.

Income tax Act 2002 has made a broad classification of income encompassing of all income earning activities. They are:

a. Income from employment.
b. Income from business, and
c. Income from investment.

The Act has defined the income heads as follows:

a. Income from employment: The income earned with the help of Labour is defined as an employment income. In other words, the payment or benefit received either in cash or kind from the employment or his/her associate in exchange of Labour are defined as employment income.
b. Income from business: Business means any industry, a trade, a profession, or the like isolated transaction with a business character and includes a past, present or prospective business. By contrast to employment, business is an earning activity typically consisting of not only the provision of labor but of the combined provision of Labour and capital.

c. Income from investment: The income earned with the help of using capital is defined as an investment income. Income Tax Act, 2058 has defined investment as an act of holding or investing one or more assets.

For the calculation of net income of these three income heads, the act has defined the incomes or amounts, which are taxable and non-taxable and expenses, which are allowed for deduction and not allowed for deduction. For the computation of income, act has made the following provisions:

4.3.1 Income from an Employment

Income Tax Act 2002, section 8, has clearly defined the incomes, which are includable in computing income from employment. An individual's income from an employment for an income year is the individual's remuneration from the employment of the individual for the year. For the purpose of computing income from an employment, the following amounts or incomes received by him in respect of any employment of services rendered by him in any of income shall be included.

a. Any wages, salary, leave pay, over time pay, fees, commission, prizes, gift, bonuses and other facilities belongs to employment.
b. Any personal allowances, including any cost of living, dearness, subsistence, rent entertainment, and transportation allowances.
c. Any payment for reimbursement of costs incurred by the individual or an associate of the individual.
d. Any payments of the individual's agreement to any conditions of the employment.
e. Any payments for redundancy or loss or termination of the employment.
f. Retirement contributions, 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 employment.
h. Other amounts includable on tax accounting or quantification, allocation and characterization of amounts.

The following amounts are not includable in computing the net income from employment.

a. Amount exempt under section 10 and final withholding payments.
b. Meals or refreshments provided in premises operated by or on behalf of an employer's employee that the available to all the employees or similar terms.
c. Any discharges or reimbursement costs incurred by the individual:
i. that serve the proper business purpose of employer or
j. That would otherwise be deductible in calculating the individual's income from any business or investment.
d. Payments of prescribed small amounts, which are so small and thus unreasonable or administratively impractical to make accounting for them. (Only upto Rs. 500 at once-expenses may be stationery, gift, tea/coffee expenses, and emergency medical expenses and pointed by department).

4.3.2 Income from Business

Income Tax Act 2002, section 7, has clearly mentioned the incomes or amounts which are includable in computing the income from business. They are:

a. Service charge (sec. 7.2)
b. Disposal of business/trading stock (Sec. 7.2)
c. Net gain from the disposal of the person's business assets or liabilities of the business (Sec. 7.2).
d. Gain form disposal of pool of depreciable assets (Sec. 7.2)
e. Prizes of gifts received by the person in respect of business (Sec. 7.2).
f. Amount received in lieu of accepting any restrictions regarding business (sec. 7.2).
g. Amount received form any investment directly related to business (sec. 7.2)
h. Income to be included due to change in accounting methods (sec. 22.6).
i. Excess amounts received due to exchange rate variation (sec. 24.4)
j. Bad debts received (sec. 25.1)
k. Proportionate amounts received under long-term contract (sec. 26.1).
l. Under payment of interest according to market rate (sec. 27.1).
m. Receivable amounts paid to others (sec. 29).
n. Amount received from compensation (sec. 31).
o. Other amounts received under the head of business income (sec. 7.2).

   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 payments (sec. 92) and
d. Dividends distributed by a controlled foreign entity at the end of the year under section 69.
e. Allowable deduction under Sec 13 to 20

4.3.3 Income from an Investment

Section 9 of Income Tax Act 2058, has defined the income received form an investment for income tax purpose. For the purpose of computing income of any person from an investment for an income year is the person's profits and gains from conducting the investment for the year and there shall be included:

a. Any dividend, interest, natural resource payment, rent, royalty, gain form investment insurance, gain from an unapproved retirement fund interest or retirement payment, made by an approved retirement fund, gain received from non-approved retirement fund or retirement payment from approved retirement fund.
b. Net gains from the disposal of the person's non-business chargeable assets of investment.
c. Excess amount of incomings over the depreciation basis including outgoing on the disposal of depreciation assets of the investment of the person.
d. Gifts received by the person in respect of investment.
e. Bad debt recovered related to investment.
f. Under payment of interest related to investment.
g. Compensation received.
h. Exchange gain.
i. Amount required to be included due to change in accounting system.
j. Income from natural resources.
k. Royalty received.
l. Rent received except from house and land.
m. Interest except received by a natural person/bank.
n. Retirement contributions, including those paid to a retirement payments in respect of investments.
o. Amounts derived as consideration for accepting restriction on the capacity to conduct the investment.

Others 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.

The act has defined the amounts, which are excluded in computing income from an investment under section 9(3). They are:

a. Exempt amount under section 10,
b. Taxation of dividend under section 54,

c. Dividend distributed by a controlled foreign entity at the end of the year under section 69 and final withholding payments, and
d. Amounts that is included in calculating the person's income from any employment or business.

4.3.4 Exemption from Income Tax

Income Tax Act 2002, has clearly defined the amounts, which are exempt and other concessions. They are described in the following section.

1. Exempt Amounts

The following amounts are exempted from tax under section 10, Income Tax Act 2002:

a. Amount derived by a person entitled to privileges under a bilateral or a multilateral treaty concluded between government of Nepal and foreign country or an international organizations.
b. Amounts derived by an individual from employment in the public service of the government of foreign country provided that.
c. The individual is a resident person solely by reason of performing the employment or is a non resident person and

2. The amounts are payable from the public funds of the country.

d. Amounts derived from public fund of the foreign country by an individual who is not a citizen of Nepal as referred to paragraph (b) or by member of the immediate family of the individual.
e. Amounts derived by an individual who is not a citizen of Nepal from employment by government of Nepal on terms of tax exemption.
f. Allowances paid by government of Nepal to widows, elder citizens, or disabled individuals.
g. Amounts derived by way of gift, bequest, inheritance or scholarship (which are including exception of business employment or investment income)
h. Amounts derived by an exempt organization by way of
    i. Gift, donation.
    ii. Other contributions that directly relate to the organization's function of the definition of exempt organization in section 2.

ii. Amounts earned by Nepal Rastra Bank as its objectives.

j. Pension received by a Nepali citizen retired from the army or police service of a foreign country provided the amounts are payable from the public fund of that country.

2. Exempt Organization

Exempt organization means:

i. A social, religious educational or charitable organization of public character registers without having profit motive.

ii. An amateur sporting association formed for the purpose of promoting social or sporting amenities not involving the acquisition of gain.

iii. a political party registered with the Election Commission.

iv. A Village Development Committee (VDC), Municipality or District Development Committee.

v. Nepal Rastra Bank.

vi. Government of Nepal.

vii. The prescribed entity that has been issued with a personal ruling under section 76 stating that to is an exempt organization.

3. Business Exemptions and Concessions

The following business exemptions and concessions are mentioned in section 11 of Income Tax Act 2002.

a. An agricultural income derived from sources in Nepal during an income year by a person, other than the income from an agriculture business derived by a registered firm, or partnership, or a corporate body, or through the land about the holding ceiling as prescribed in the Land Act 1964, is exempted form income tax.

b. Incomes derived by co-operative societies, registered under Cooperative Act 1991, from business mainly based on agriculture and forest products such as agriculture and silk production, horticulture and fruit processing, animal husbandry, dairy industries poultry farming, fishery, tea gardening and processing, coffee farming and the other processing, herb culture and herb processing, vegetable seeds processing, bee- keeping, honey production, rubber farming, floriculture and production and forestry related business such as lease- hold forestry, agro-forestry, cold storage of established for the stores of vegetables and business of agricultural seeds, insecticide fertilizer and agricultural tools (other than machine operated) and rural community based saving and credit co-operatives are exempt from tax. Dividends distributed by such societies are also exempted from tax.

c. Income derived from sources in Nepal during an income year by a person from a special industry is taxed as follows:
    i. The industry provides direct employment to 600 or more Nepalese citizens throughout the year, 10 percent rebate is provided to the special industries or 90 percent of rate is applicable to that income for the period of forever.
    ii. The special industry operated in a underdeveloped, undeveloped, highly undeveloped and remote zone, at 90, 80, 75% and 70 percent respectively, of the rate is applicable for the period of ten years from commencing and including the year in which the operation commences.
    iii. The special industries based on information technology established in an information technology (IT) park like Banepa, 25% rebate is provided on existing rate for forever.
d. A person who is entitled to concession under subsection a, b or c shall calculate the income referred to in those subsections as though the income was the only driven by a separable.
e. When a person qualifies for more than one concession under subsection (b) I or II with respect to the some income, the person shall only be entitled to one concession with respect to that income but shall be entitled to select which concession applies.

4. Donation gifts to exempt organizations:

Section 12 of Income Tax Act 2002 has mentioned the provisions of donation gifts to exempt organization. The provisions are:

a. A person may claim to have his taxable income for an income year reduced by donation gifts made by the person during the year to an exempt organization, that are approved for the purposes of this section by the department.

b. Donation made to an exempt organization, approved by Inland Revenue Department (IRD) is allowed for reductions from taxable income. Reductions allowed to an individual or an entity will not exceed Rs. 100,000 or 5% of adjusted taxable income. 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 expense incurred for special purpose or donation given by the person.

c. Donation given to national political parities up to Rs. 50 lakhs before three months of election is deductible expenses from taxable income. Likewise donation given to Lumbini Development fund and Pashupati Development Fund up to Rs. 10 lakhs is tax exempt amount.

4.3.5 Allowable Deductions

Income tax Act 2002, Sce. 13 to 20 have described the allowable deductions which are as follows.

1. General deductions (Sec.13)

To calculate a person's income from any business or investment for an income year the following expenses incurred in the transaction can be deduct.

a. Incurred during the year.
b. Incurred by the concerned person.
c. The expenses which is incurred to produce income from business or investment.

2. Interest expenses (Sec.14)

To calculate a person income from any business or investment for an income year the interest expenses incurred by the person can be deduct in following conditions:

1. The borrowed money is used in the year.
2. If the money borrowed to purchase an assets, and the assets must be used in the business in the same year.
3. In other case borrowed money is used to generate income from business or investment.

In case of resident entity controlled by tax exempted institution and that entity has paid interest to the controller institution or related person, the resident entity may deduct the

Interest paid without exceeding the sum of follows (a + b)

a. Total interest derived by that entity which is included in the taxable income, and
b. 50% of the entity's adjusted taxable income for the year calculated without including any interest income and without deducting any interest expenses paid by the entity.

The portion of interest expenses which is not allowed to deduct during the income year because of the limitation. So, remaining portion will be deducted in the next income year.

For this purpose, the controller entity means the institution holding 25% or more of equity or managerial power at any time during the income year.

Here, tax exempted entity means:

a. Tax exempted and related person.
b. Entities getting business concession and facilities under (Sec.11)
c. Non-resident person or his related person or
d. Any combination of (a), (b) and (c).

3 .Cost of trading stock (Sec.15)

Cost of trading stock is allowed to deduct while calculating income from business or investment.

Raw material, work- in progress and finished goods are included in the trading stock.

Cost of trading stock=opening stock + purchase during the year- closing stock.

- For valuation of the closing stock cost price or market price whichever is less is taken.
- The person keeping accounts on cash basis can adopt either prime cost or factory cost for the valuation of trading stock.
- The person keeping account on an accrual basis must adopt factory cost basis for the valuation of trading stock.
- Absorption or prime cost can be derived as follows:

- Prime cost = Direct material cost + direct labour cost + factory variable overhead cost
- The factory cost is derived as follows:
- Cost of raw material consumed + direct labour cost + factory overhead (fixed+ variable)
- Repair and improvement expenses and depreciation of plant and machinery should be added while calculating the factory or variable factory overhead (Kandel, 2003, 68)

4. Repair and improvement cost (Sec.16)

For the purpose of calculating a persons income for an income year from any business or investment, repair and improvement cost of depreciable assets, owned and used by the person should be deducted which is incurred during the year.

However, according to the Act, such costs do not exceed 7% of depreciation basis of assets pool at the end of the income year.

If the actual repair and improvement cost is more then 7% of the assets pool, the balance amount is capitalized and added to the depreciation basis then written off in the next year.

Repair and improvement cost can be calculated as follows:

Depreciation basis = Opening written down value of assets pool plush last years capitalized part of the assets plush addition of the assets during the year minus disposal of assets during the year.

7% of depreciation basis or actual repair and improvement whichever is less is allowed for deduction.

5. Pollution control cost (Sec.17)

Pollution control cost means cost incurred by a person in the possess that seeks to control or protect and conserve the environment.

a. To calculate a person income for an income year from any business, the pollution control cost can be deducted that is incurred during the year in conducting the business.
b. But the lower amount of the below is allowed for deduction.

- Actual pollution control cost or
- 50% of adjusted taxable income from all business.

The portion of pollution control cost not allowed for deduction will be capitalized at the beginning of the next income year under block ‘D’ of assets pool.

Government has a will of controlling pollution to protect environment but has not spent a little bit money on it.

6. Research and development cost (Sec.18)

Research and development cost means cost incurred by the person for the purpose of the developing and improving the business system, process and products etc.

Research and development cost though the capital nature are allowed for deduction to an extent from taxable income of the person.

The lower amount of the below is allowed for deduction:

a. Actual research and development cost, or
b. 50% of adjusted taxable income of all business.

The portion of research and development cost not allowed for deduction in the income year is capitalized at the beginning of next income year under the block “D” of assets pool.

Here, adjusted taxable income of a person for an income year is the taxable income without reducing donation (Sec.12) and without deducting pollution control cost (Sec.17) and research and development cost (Sec.18).

7. Depreciation allowance (Sec.19).

Depreciation is the gradually decreasing in the value of assets due to wear and tear, obsolescence or the passing of time.

Depreciation at prescribed rate is allowed to deduct on used depreciable assets owned by the person or organization.

There are different rate of depreciation for different blocks 5% for “A” group, 25% “B”, 20% for “C”, 15% for “D” and original cost by useful life for “E”.

The depreciation basis (pool-wise) is calculated as.

Opening WDV plush additional during the year minus disposal during the year.

The following entities allowed deducting additional one third of the prescribed rate of assets falling under A, B, C and D blocks.

- Entities engaged in building public infrastructure to transfer to the government and any other entities engaged in power generation, transmission or distribution of electricity.
- Entities fully engaged in operating special industry.
- Entities fully engaged in operating road, bridge, tunnel, ropeway or flying bridge constructed by the entity.
- The entity fully engaged in operating trolley bus or train.
- The entity who earned income from export business in an income year.

An individual can not get such facilities even though, she/he is operating similar activities.

8. Loss Recovery (Sec. 20)

For the purpose of calculating a person's income from an income year from any business or investment there can take place different losses in business or investment. When losses incurred in business of domestic source, those losses can be set off and carry forward upto 7years from any business income situated within the country or outside the country. In the case of electricity projects involving in business power station, generating and transmitting electricity and the projects conducted by any entity so as to build public infrastructure, own operate and transfer to the government, any unrelieved loss of the previous seven years can be deducted.

When losses incurred in investment of domestic source, those losses can be set off and carry forwarded upto 7 years from any incomes of investment within the country or outside the country only.

Where a person may deduct an unrelieved loss in calculating the person's income for an income year from more than one business or investment, the person may prioritize in which calculation the loss or part of the loss is deducted.

4.3.6 Expense not Allowed for Deduction

To calculate the income of a persons' for an income year from any business, employment, or investment, the following expenses are not allowed for deduction under section 21 of Income Tax Act 2002.

a. Personal nature or domestic expenses.
b. Income tax paid, fines and penalties.
c. Expenses incurred for acquiring tax free income and final withholding payments.
d. Cash payment in excess of Rs. 50,000 at a time by a person having annual transaction more than Rs. 20 lakhs (2 million) except in certain circumstances.
e. Distribution of profits by an entity for example dividend distribution to the shareholders.
f. Expenses not related to earning of income.
g. Any reserve, provision or fund.
h. Expenses of capital nature.
i. Foreign income tax.
j. Other expenditures not exempted as admissible.

A person whose annual turnover for an income year exceeds Rs. 20,00,000 is not allowed a deduction for a cash payment in excess of Rs. 50,000 incurred at once other than in the following conditions by the person during the year, if:

a. Payment made to government of Nepal, a constitution body, a corporation owned by the government of Nepal, or a bank or financial institution,
b. Payment is made to a farmer or producer producing primary agriculture products even in the case where the product is primary processed by the farmer himself,
c. Payment is a retirement contribution or retirement, payment,
d. Payment is made in an area where banking services are not available. An area having banking services means the area where there are no banking facilities within the surrounding of ten kilometers.
e. Payment is made and must necessarily be made in cash or on a day when banking services are closed.
f. Payment is made into a bank account of the payee.

Any other amounts, to the except to which a deduction is not denied by section 21: (1) (f), has not defined the amounts. This kind of provision will provide a loophole for both tax administration and taxpayers.

CHAPTER-V
MAJOR FINDINGS, CONCLUSIONS AND RECOMMENDATIONS

5.1 Major Findings

According to the preceding chapters, some important findings can be drawn. Major findings of this research study are summarized below:

1. The government revenue comes from two sources internal sources and external sources. Internal sources include both tax revenue and non-tax revenue. Tax revenue is dominating to non-tax revenue of Nepalese government. The contribution of tax revenue shows the increasing trend which contributed 77.97percent in FY 2001/02 on the total revenue and it was increased to 80.85 percent in FY 2008/09.
2. The average collection of total tax revenue, non-tax revenue and total revenue were Rs. 62503.38 million, Rs. 16627.80 million and Rs.79131.30 million respectively whereas average percentage collected tax revenue and non-tax revenue were 78.98 percent and 21.02 percent respectively during the study periods of 8 years.
3. The contribution of total direct and indirect tax to total tax revenue were 23.73 percent and 73.06 percent in FY 2001/02 where as the contribution of direct tax was increased to 28.96 percent in FY 2008/09 but the contribution of indirect tax was decreased to 71.04 percent in FY 2008/09.
4. The average collection of direct tax and indirect tax were Rs.16411.82 million and Rs. 46091.63 million respectively, and the average percentage of direct tax and indirect tax on total revenue were 26.26 percent and 73.74 percent respectively during the study periods of 8 years.
5. The average tax collection of total indirect tax viz. custom duties, excise duties and VAT during the study periods were Rs.16796.43 million, Rs.7767.14 million and Rs. 21528.06 million respectively and average percentage on total indirect were 37.35percent, 17.26 percent and 45.39 percent respectively.
6. The average tax collection in direct tax viz. income tax, house and land registration fees, vehicle tax and other tax during the study periods of 8 years were Rs.11651.52 million, Rs. 2187.87 million, Rs 920.84 million and Rs

744.47 million respectively whereas average percentage on the same were 77.39 percent, 13.33 percent, 5.65 percent and 4.15 percent respectively.

7. The average percentage of direct tax on tax revenue, GDP and total revenue were 25.83 percent, 2.63 and 20.32 percent respectively during the study periods of 8 years.
8. The average percentage contribution of income tax on direct tax, tax revenue, total revenue and GDP were 77.39 percent, 18.64 percent, 14.72 percent and 1.92 percent respectively during the study periods.
9. Nepalese tax revenue is the composition of direct and indirect tax revenue. But there is dominant role of indirect tax revenue in Nepalese tax revenue. The contribution of direct and indirect tax revenue were 26.94 percent and 73.06 percent respectively in FY 2001/02 whereas 28.95 percent and 71.04 percent in FY 2008/09. It shows that contribution of direct tax is increasing trend (i.e. 26.94% to 28.95%) whereas contribution of indirect tax is decreasing trend (i.e. 73.06% to 71.04%).
10. the contribution on total direct tax, total tax revenue, total revenue and GDP were 84.01 percent, 22.63 percent, 17.65 percent and 1.94 percent respectively in FY 2001/02 where as same were 72.42 percent, 20.97 percent 16.95 percent and 2.55 percent respectively in FY 2008/ 09.
11. The total tax revenue on GDP (i.e. tax/GDP ratio) of Nepal is not satisfactory. It has never exceeded 13 percent from 2001/02 to 2008/09. In 2001/02, the total tax/GDP ratio was only 8.60 percent, which exceeded to 12.20 percent in FY 2008/09. This shows the increasing trend to tax/GDP ratio in slower pace.
12. Income tax is the composition of corporate income tax, individual income tax, and investment income tax. Corporate income tax is collected from government corporations, public and limited companies, partnership firms. Individual tax is collected from remuneration and industry, business and profession. Investment income tax is collected from dividend tax, interest tax, royalty tax, rent tax etc.
13. the contribution of corporate income tax, individual income tax, house and land tax and interest tax were Rs 3181.34 million, 4419.09 million, 2.29 millions and 467.70 millions respectively in FY 2001/02 where as the contribution of same were Rs 8316.45 millions, Rs 8608.65 millions Rs 00 millions and 1783.35 millions in FY 2008/09.

14. All incomes generated by an individual are not taxable income. because the minimum cost expenses required for living can not be taxed. So, from the commencement of income tax in Nepal, some extends of amounts are exempted from income tax. This extent is known as exemption limit. Income tax exemption limit in Nepal has been changing on the basis of time and condition. It was Rs 7500 for an individual and Rs 10000 for a couple or family in FY 1979/80-1980/81 which is increased to Rs 160000 for an individual and Rs 200000 for a couple or a family respectively in FY 2009/10.
15. The income tax rates and slabs have been changed radically in recent years. Personal income tax rates, which ranged from 7 percent to 60 percent in seven slabs in 1975/76, (Table 4.11) was reduced to only two rates i.e. 15 percent upto Rs. 85000 and 25 percent of the rest amounts in 2008/09. Similarly, the corporate income tax rate has been reduced from 60 percent in FY 1975/76 to 30 percent (For banking and financial companies and firms), 25 percent (for other including partnership firms) in 2000/01 and 20 percent (for special industries) in 2008/09.
16. In Nepal, the coverage of income tax base is low. Agricultural income is exempted from income tax. Exclusion of agricultural income from the tax net alone cuts out about half of the GDP. In the other hand, employment income is taxed more heavily than the capital income. Retirement amount received by Nepalese people being retired from the service by army or police of foreign country is also exempted from income tax. Such provision provides loopholes for tax evasion.
17. Some exemptions granted to achieve certain objectives are not effective. Tax incentive is one of the example. Although tax concessions encourage the establishment of industries in certain areas but they vanish or change names, ownership or place of the business when the tax incentives facility expires.
18. Income tax act has clearly mentioned the organizations, which are tax free which is called exempt Organization. Act has exempted a social, religious, educational or charitable organization of a public character registered without having profit motive.
19. Donation made to an exempt organization, approved by Inland Revenue Department (IRD) is allowed for deduction from taxable income. Deduction allowed for an individual or an entity will not exceed Rs. 100,000 or 5% of

adjusted taxable income. 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 expense incurred for special purpose or donation given by the person. Here, the act has not defined "What is special purpose?"

20. Donation given to national political parties upto Rs. 10,00,000 before three months of election and donation given to Lumbini Development Fund and Pashupati Development Fund upto Rs. 10,00,000 is deductible expenses from taxable income. From the above provision it is clear that the donation given to political parties is allowed for deduction but it has not been able to solve the voice of people of 'transparency of donation amount given by business to political parties.'

On the basis of empirical analysis some major findings can be drawn which are summarized as follows

1. 58 percent of the total respondents were that the contribution of income tax to national revenue of Nepal is not satisfactory.
2. 58 percent of the total respondents were believed that the income tax administration of Nepal is unsound and ineffective.
3. Most of the respondents believed that the main causes which are responsible for the creation of unsound and inefficient income tax administration of Nepal were weakness in government’s economic policy, less public participation, lack of trained employee, inefficient organizational structure of the tax administration, complicated tax laws and provisions etc.
4. Most of the respondents believed that the income tax rate in Nepal is medium.
5. 54 percent of the total respondents were believed that the exempted items of income are sufficient under the income tax Act 2002.
6. 68 percent of respondents were believed that the current income tax exemption limit is not adequate and most of the respondents suggested to increase the exemption limit to Rs 220000 for an individual and Rs 275000 for a couple or a family.
7. 60 percent of the total respondents thought that the exemption limit should not be provided according to the number of dependents and rests were in favor of it.

8. 68 percent of the total respondents were agreed that the exemption limit should be adjusted according to the inflationary situation of the country.
9. 64 percent of the total respondents were in favored to exempt the agricultural income where as 12 percent of respondents thought that it should not be exempted and 16 percent of respondents were in favor to treat the agricultural income as other income.
10. Majority of the total respondents were believed that the itemized deductions of expenses are not sufficient under the income tax Act 2002.
11. According to the economic condition and per capita income of the country, current additional tax exemption limit (Rs 30000, Rs 24000, Rs 18000, Rs 12000 and Rs 6000 to remote area A, B, C, D, and E respectively) to the individual working in different remote area is proper or suitable.
12. Majority of the respondents were agreed that the special industries established in remote, undeveloped and underdeveloped area of the country get additional tax exemption facilities i.e. 30 percent, 25 percent and 20 percent of tax rate respectively and it is applicable for 10 income year is proper or suitable at present.
13. Most of the respondents were believed that the major problem and weakness of the Nepalese income tax system were lack of clear provision under the income tax law, difficult to maintain the account for tax purpose, lack of timely adjustment of tax law, ambiguous provision in income tax law and limited tax base etc.
14. 54 percent of the total respondents were believed that the exemption and deductions under the Nepalese income tax Act is not sufficient in all aspects where as 46 percent of respondents were agreed that the exemption and deduction under the Nepalese income tax is sufficient in all aspects.

5.2 Conclusions

Developing countries like Nepal is facing serious problems in the process of economic development. Lack of sufficient financial resource and its efficiency is the main constraint for economic development of Nepal. Sufficient funds are required to meet the objectives of economic development. But, Nepal has not been able to collect necessary funds or revenue. Due to poor performance on internal revenue collection and its mobilization, Nepal has been heavily relying or foreign loans and grants. Thus the dependence is increasing day by day, which is not desirable for any economy. Thus, it is the most necessary to mobilize the internal fund or revenue to the optimum level.

To increase the government internal revenue, Nepalese government is trying to extract money from people through taxation. Within tax, income tax is the most important source of government revenue, which is considered as a good remedy to cure growing resource gap in Nepal.

In Nepal, the history of income tax is not so long. It was started only on late fifties. The income tax was introduced as a trial on business profit and the remuneration income. The first elected government levied the first income tax and no specific act was made to define and treat income tax. The first income tax act was introduced only in 1959/60, since then four income tax acts has been implemented. From the very beginning the concept of exemptions, deductions and other forms of tax relief in income tax have emerged in Nepal. All incomes of an individual can not be taxable income because the minimum cost required for subsistence can not be taxed. The exemptions, deductions and other forms of tax relief are essential to encourage an individual to work more. The tax relief works as an incentive to an individual. So, the concept of exemption, deductions, and tax relies were emerged in Nepal from the very beginning of income tax.

Exemption limit and the rate of the income tax is determined according to the income level and sector wise but has not been adjusted according to the inflationary situation of the country and number of dependents.

Income tax system of Nepal has been blamed as being inefficient system. Being various problem relating to income tax, revenue collection from income tax is low as compared to other developing countries like India, Sri Lanka, Pakistan etc. Nevertheless, if the data are analyzed relating to it, it is found that it is neither bad nor worse but it is has been continuously improving. However, income tax laws and administration in Nepal are to be deeply scrutinized and properly implemented. The provisions made on the act have to be mentioned clearly and language has to be made clear some reforms in tax administration are needed. If the problems relating to income tax system in Nepal can be solved and resources are effectively utilized then only the prospects of revenue collection through income tax will be effective and bright and the economic development of Nepal will be achieved.

5.3 Recommendations

As earlier described, there are various problems regarding to income tax of Nepal. The existing tax assessment procedure is also unsound and inefficient. The major causes of being unsound and inefficient tax assessment procedure are weakness in government's economic policy, lack of public participation, complicated tax laws and provisions, lack of trained and competent employees etc. In the opinion survey, it was noticed that most of the respondents were dissatisfied with the government economic policy and lack of public participation. The study mostly focused into the problems that are related to exemption and deduction. So, the recommendations made for other than the exemptions and deductions may be considered as the general recommendations. Hence, the research of the study has made the following recommendations on tax exemption and deduction.

Exemption

1. To increase the income tax revenue, the present tax base must be widened by including the incomes from agricultural sector; retirement amount received by Nepalese people being retired from the services by army or police of foreign country and currently exempted other sources income.
2. In the agricultural income, there should be some exemption limit and the income above this limit should be taxed.
3. The present provision of an individual and a family exemption limit are not appropriate. It should be raised to a minimum of Rs. 190000 for individual and Rs. 230000 for a family.
4. The exemption limit should be adjusted according or the inflationary situation of the country of yearly basis.
5. There are many provisions relating to tax exemptions and concessions. Some concessions granted to achieve certain objectives are not effective. Tax concessions encourage the establishment of industries in certain areas but they

vanish or change names, ownership or place the business when the concession facility expires. The incentives provided to special industries are not effective. Such kinds of concession do not encourage to open the industry in remote areas,. For the purpose of industrial development of remote area, a separate special package should be introduced.

6. Few percentages of tax rebates should be provided to the taxpayers who submit true income statement within the specified period of time.
7. Income tax on total export amount is not appropriate because income tax should be based on income not on the total amount. So, the provision of taxing on export income should be introduced. Similarly, export fee on export transaction should be eliminated or exempted.
8. Double taxation on dividend should be eliminated.
9. Income Tax Act has mentioned the organizations, which are tax free (exempt organizations). Act has exempted a social, religious, educational or charitable organization of a public character registered without having profit motive. In the case of non-transparent private business like boarding school, NGO's or other entitles, where profits are earned, but for the sake of tax planning, is called retained earning or something else. So, they should new take into tax net.
10. Retirement Contributions are nothing else than the product of sacrifice of present earnings. There are the bases for living standard of oldness of employees. So, they should be excluded from income tax.
11. Dearness allowance is given to meet the living standard of employees, it is not lawful to include in taxable income. So it should be fully exempted from income tax.

Deduction

1. Donation given to a political parties registered with the election commission is allowed for deduction. But it has not been able to solve the voice of people of 'transparency of donation amount given by business men to political parties'. So, donation amount given to political parties should be transparent.
2. Deductions allowed from an employment income are not sufficient. So, the following deductions should be provided to the tax payers whose sources of income are only the remuneration.

a. Expenses for better education of their children.
b. Medical expenses made by taxpayers.
c. Expenses made for house rent.
d. Educational expenses for taxpayers himself if he is still studying in an educational institution.
e. Maximum amount of Life insurance premium should be allowed for deductions.
f. Pregnant delivery expenses for certain limit.

3. Clear provisions should be made in the case of deduction. All the items of deductions should be clearly defined in the act.
4. Deductions allowed from business or investment incomes are not sufficient. So the following deductions should be provided to the taxpayers. Whose source of income is business or investment.
   a. In the case of exempt controlled resident entity, full deduction of interest expense is not allowed. It is not lawful step to the businessmen who operate the business with loan or debt amount. So, it should be full allowed for deduction within an income year.
   b. The provision of adding any excess lose or part thereof repair and improvement costs to the depreciation basis amount is not contextual and lawful provision because it shows that the repair or improvement cost of a depreciable asset has not got full approval or deduction. So it should be fully allowed for deduction within an income year.
   c. To control pollution and protection of environment, environmental protection is more essential and should be expended on it, expenses made on it should be approved and should be fully allowed for deduction within an income year. Act should not make standard limit on it.
   d. For successful industrial development, research and development is more essential and should be expended on it. Expenses made on it should be approved and should be fully allowed for deduction within an income year. Standard limit on it should not be made.
   e. There should be specific provision of depreciation of assets, which are taken on lease and installment basis. Act should not be silent on it.

Provisions made on depreciation allowances should be generally understandable by all people.

f. Carry forward of losses for 7 years is not sufficient as compared to other countries. So, it should be extended up to 9 or 10 income years. The provisions of carry backward of losses should be considered because the accounting system of Nepal is not so standard to apply this provision.

Besides this recommendation, the following recommendations are made to compensate the loss of revenue due to the provision of additional exemption and deductions recommended by the researcher;

1. The income tax policy should be formulated so as to match with the economic policy of the country.
2. The members involved in formulating income tax policies must have deep knowledge about income tax.
3. Timely revision and adjustment should be made in the matter of income tax policy.
4. Income tax policy should be formulated so as to satisfy the following criteria:
    a. It should be progressive ensure social justice.
    b. It should be consistent with tax administration capacity.
    c. It should not influence to prevent against national priorities and efficient resource use.
5. The success or effectiveness of any system entirely depends upon implementation of provisions, which is the major responsibility of administration. In Nepal, one of the most important reasons to be unsound income tax system is inefficient and unscientific income tax administration. The following recommendations are made for the improvement of income tax administration in Nepal:
    a. All the tax personnel should be given comprehensive training on various aspects of taxation on regular basis. For this, a separate training section within tax department should be established.
    b. The performance, responsibilities, authorities and duties should be clearly defined.

c. Financial benefits and extra incentives should be provided to the personnel to decrease corruption.
d. Effective reward and punishment system should be established.
e. Working environment of the tax offices should be improved, other facilities should be provided.
f. The administration should try to increase effective public participation to minimize the income tax evasion.
g. Income tax experts/profession should be increased in tax administration.
h. Coordination between staffs and departments should be established.
i. Delays in assessment should be reduced as soon as possible.
j. Fair and scientific provision of promotion and carrier development should be introduced.
k. The cost of revenue collection is one of the determinant of administrative efficiency. So, the concerned authority should pay due to attention on it.
l. An integrated information system should be developed to prepare the list of potential taxpayers and gather information of various aspects relating to income tax.
m. The system of recording by computer should be developed in income tax administration.
n. Tax education should be provided to taxpayers on regular basis.

6. Laws relating to income tax should be clear, simple and comprehensive, it should not contain any loopholes and ambiguity; therefore it should be reviewed frequently and reformed. The following recommendations made for the reformation of existing tax laws in Nepal as;
    a. The language should be simple and clear. In spite of using the vague meaningful words, clear cut provision should be undertaken.
    b. The definition made in Income Tax Act should be further clarified and well defined.
    c. The assessment and tax collection provisions should be made clear and simple.
    d. The provision of fines, penalties and punishments should be made at higher rate for income tax evaders.
    e. The assessment of time limit after the submission of income statement should be reduced.

f. Discretionary power of the tax officers should be curtailed and their rights and duties should be clarified in Income Tax Act.

7. The reward, prize, incentives provisions should be introduced in the act to encourage the taxpayers to pay tax voluntarily rather than coercive measures.
8. Clear provisions should be made in the case of deductions. All the item of deductions should be clearly defined in the act.
9. There should be compulsory provisions of auditing.
10. The administrative should pay great attention to bring the income from house and land rent, doctors clinic, consultancy services, tuition center etc into income tax net. In these sectors income tax has been highly evaded.
11. Unnecessary political and outsider's pressure should be avoided.
12. The provision of tax deduction at source and advance payment to tax should be extended to different source of income as far as possible.

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Appendix

Questionnaires

Income Tax in Nepal:

A study of Exemptions and Deductions

Name of the respondents:…………………..

Position ……………………………

Department ………………………..

Tenure of service………………….

(Please tick your answer in the following and put in order of preference from first to last number if there are more than four alternatives)

1. Do you think that contribution of income tax to national revenue of Nepal is satisfactory?

   (a)Yes (b) No

2. Do you think that the income tax administration of Nepal is sound and efficient?

   (a) Yes (b) No

3. Which are the responsible for the creation of unsound and inefficient income tax administration of Nepal?
   a. Defective assessment procedure. (…….)
   b. Lack of public participation. (…….)
   c. Lack of tax education. (…….)
   d. Lack of trained and competent employees. (…….)
   e. Inefficient tax administration. (…….)
   f. Weakness in government economic policy. (…….)
   g. Inefficient organizational structure of tax administration of tax structure. (….)
   h. Complicated tax laws and provisions. (……)
   i. Corruption. (……)

4. What is your opinion about current income tax rate?

(a) High (b) Medium (c) Low

5. Do you think that the exempted items of income are sufficient?

(a) Yes (b) No

If No what kind of income should be exempted? Please note in order

(a)…………. (b)………….. (c) …………..

6. Do you think that the current income tax exemption limit is adequate?

(a) Yes (b) No

If No which of these exemption limit do you suggest for an individual and for a couple or a family?

For an individual

(a) Rs 190000 (b) Rs 200000 (c) Rs 220000

For a couple or a family

(a) Rs 230000 (b) Rs 245000

(c) Rs 260000 (d) Rs 275000

7. Do you agree that family exemption limit must be provided according to the number of dependent?

(a) Yes (b) No

8. Do you think that exemption limit should be adjusted according to the inflationary situation of the country?

(a) Yes (b) No

9. What is your opinion on exemption providing on agricultural income?

Options

a. Yes, it should be exempted
b. No, it shouldn't be exempted
c. It should be treated as other income
d. Other, (if any, specify)

10. Do you think that the itemized deductions are sufficient?

(a) Yes (b) No

If No what kind of expenses should be deducted while computing taxable income?

a. ……….
b. ………
c. ……...
d. ………

11. Is it suitable that the additional exemption given to an individual who is working in the different remote area?

(a) Yes (b) No

12. Is it suitable to provide additional facilities to the special industries established in the different areas in the country?

(a) Yes (b) No

If No how much additional tax exemption should provided?

13. What are the major problems and weakness of the Nepalese income tax system?

- Lack of trained employees. (……)
- Lack of co-operation with tax administration. (…….)
- Increased corruption. (……)
- Lack of tax education. (……)
- Difficult to maintain the account for tax purpose. (…...)
- Lack of timely adjustment of tax law. (……)

- Limited tax base. (…….)
- Ambiguous provision in income tax law. (…….)
- Relatively high tax rate. (……)
- Lack of clear provisions under the income tax law. (……)

14. Are the provision relating to exemptions and deductions under the Nepalese income tax Act 2002 sufficient in all aspects?

    (a) Yes (b) No

If No which aspects the improvement are need?

a. ……………
b. …………...
c. ……………

15. Do you have any suggestions about income tax in Nepal?