

CHAPTER I

INTRODUCTION

1.1 Background of the Study

Nepal, being developing country as well as agriculture base country. The government of Nepal is trying to raise the living standard of people conducting various economic development activities. For this our country needs to manage the various resources like: man, money, machine and materials. To obtain this particular resources government receives income through internal and external sources. Revenue mobilization also counts as the very important feature of government. The income of government is called revenue. Government revenue also known as public revenue is money received by a government. It is an important tool of the fiscal policy of the government and it is the opposite factor of government spending. Revenues earned by the government are received from different sources such as tax levied on the incomes and wealth accumulation of individuals, corporations, on the goods and services produced, exported and imported from the country, non- taxable sources such as government-owned corporations income, central bank revenue and capital receipts in the form of external loans and debts from international financial institutions. Government needs revenue carry to implementing activities. Such activities are included in the government annual budget. Budget is the composition of revenue and expenditure. Public expenditure is spending made by government of a country on collective needs and want such as pension, provision, infrastructure etc., until the 19th century, public expenditure was limited as laissez faire philosophies believed that money left in private hands could bring better returns. The role of public expenditure is in determining levels of income and distribution in the economy. Keynes J.M (1936).

Tax simply means a liability to pay an amount to the government. It is a compulsory contribution to the national revenue from the taxpayers according to law. Findlay's shires defined tax as " A compulsory contribution from a person to the government to defray the expense of the government which have been incurred from the public good without references to special benefits" (Agrawal, 2006).

In this way, it is clear that a tax is a compulsory level and those are taxed has to pay it without getting corresponding benefit of services and goods from the governments. The taxpayers do not have any right to receive direct deposit from the tax paid.

The government's revenue is mainly divided into two types. They are non-tax revenue and tax revenue. Non-tax revenue or non-tax receipts are government revenue not generated from taxes, consists of service charge, fees, penalties, interest, dividend and royalties etc. A tax is a financial charge or other levy imposed upon a taxpayer (an individual or legal entity) by a state or the functional equivalent of a state such that failure to pay is punishable by law. Taxes are also imposed by many administrative divisions. Taxes consist of direct or indirect taxes and may be paid in money or as its labor equivalent. Customs duty, excise duty, income tax, value added tax, vehicle tax and property tax are the major components of the revenue. Tax revenue is broadly divided into two types. They are indirect tax and direct tax. Distinction between direct and indirect tax is based on the impact and incidence of tax. The direct tax is the personal tax. If the impact and incidence is borne by the same person whom it is legally imposed and there is no possibility of shifting, then it is called direct tax. Examples are income tax, profit tax, interest tax, dividend tax, property tax etc. On the other hand, indirect tax is commodity and services based tax. If any is legally imposed on one person but the incidence of the tax is borne by another person through backward and forward shifting process. Then it is called indirect tax. Value added tax (VAT) customs duty and excise duty are some examples of indirect tax. Through taxation, the government can increase revenue as well as affect consumption, production and distribution pattern of the economy. Taxation has been taken as the best effective instrument of fiscal policy for raising the ratio of saving to GDP. In order to meet the growing need of public expenditure, the government has to generate resources from the various sources. The sources of government revenue are mainly of two types. They are internal and external sources. (Adhikari, 2005).

Since being a major source of funds, tax collection should be more flexible to achieve maximum social and economic objectives. Collections of taxes help in redistribution of financial resources means by the transformation of wealth from person with higher economic level to lower economic level. Providing incentives and concessions in income tax for promoting industries in backward areas may also reduce regional economic imbalances. It has become an effective instrument to ensure balanced socio-economic growth (Lamsal, 2006).

Regarding the Nepalese tax administrative problems , the government of Nepal has done through implementing income tax act (ita) , 2058 in which , Nepalese tax administration has been attempting to modify itself to meet the pressing challenges brought change in technology and economic policies. However, still its working procedures are traditional and the cost of administration hasn't been brought to the satisfactory level. ITA 2058 is blamed that the law is complicated, vague and their needs the effort for simplification of the law that can be used in practical easily. If the tax laws fails to be par with the international tax norms also. It will not be able to attract the foreign investment. The tax law be coherence with the economic situation of the country (Lamsal, 2006).

The effectiveness of tax system depends on the existing management and leadership. A vigilant and transparent tax administration and capacity of timely reviews in policy backsliding would be a pre- requisite for sustaining the gain in the revenue front. The realization of sincere and active support of officials involved and taxpayers affected should remain always in high priority in the administration. The study is focused to analyze the structure of income tax and its administrative aspect .the existing Nepalese tax system has many problem. inefficient customs valuation system , feeling of the people towards tax as a punishment , leakage in tax , lack of taxpayers awareness , lack of tax culture , lack of accuracy and utility in accounting system . Low tax base, high tax rate, weak tax administration, many loopholes in tax law are some of the problems. Nepalese income tax has low level of contribution to its total internal resources mobilization owing to those problem these problems should be adequately addressed to potentials the income tax (Lamsal, 2006).

Having all existing reasons mentioned in above, the problem and prospects of tax administration in Nepal must be reviewed. Tax administration is the diver of whole tax system. It moves the whole system of government and country to the right direction. The main focus of the study is growth rate, contribution of tax revenue, contribution of government revenue with foreign grant and without foreign grant.

1.2 Statement of the Problem

In own aspect and condition of the developing countries in the world. Nepal has been suffering from resources constraints, massive poverty, rapid growth of population increasing frictional and seasonal unemployment, disease aggressive dependent on the

agricultural, subsistence living standard and poor infrastructure despite over five decades planned development efforts. The government has to allocate large amount of money to uplift the socio- economic status of the people. Hence the government expenditure is growing. So, government revenue must be increased. Income tax is the best source of government revenue .It is good in the sense that only capable tax payer has to pay income tax. Income tax is powerful instrument for mobilizing internal resources. It is also instrument of economic growth and social justice.

Nepal is facing the problem of rising tendency of government expenditure. Its gross domestic product (GDP) per capita is reach at \$752 (Economic Survey, 2016). It is the lowest in the south Asian association for the regional cooperation (SAARC) countries. So Nepal needs to huge amount of capital for economic development. Despite the various measures adopted by the government to boost revenue collection, there is still a substantial resource gap between expenditure and revenue. The rate of government expenditure is exceeding the rate of growth revenue collection almost every year from the beginning of its development phase. The sources of filling the resources gap are internal and external borrowing. Now days the internal borrowing has been playing importance role to fulfill the resource gap. In FY 2015/ 2016, the internal borrowing was Rs 233.4 billion which stands 10.3% of the internal to GDP ratio. It doesnot indicate favourable to the economic growth of country (Economic Survey, 2016).

Taxation is considered as one of the most important part of government receipts. It plays an important role in domestic resource mobilization. Through the taxation, resource of the private are transferred to public sector for the economic development has been the major concern of very developing country. In newel, social and economic development is not progressively and sufficiently reached at target point as it has a small economy with limited resources and political instability. Polices and strategies have been largely in effective. Dependency over foreign aid is dramatically increasing so the deficit of budget is at a peak level (Lamsal, 2006).

Nepal is developing country, facing a serious problem of resource gap. Dependency on foreign assistance is continuously, increasing resource gap can be narrowed either by curtailing government expenditure or by increasing government receipts. Curtailing government expenditure is not easy task. Increase in regular expenditure can be reducing to some extent. Nepal spends 10.3% of the regular expenditure for the payment of principle and interest of its debt (Monetary Policy, 2016/17). Other

regular expenditure has been rapidly increasing. Resource is needed to fulfill development activities, social services and to maintain the infrastructures already built.

The development of a nation will be possible where the government can mobilize its own internal revenue, which contributes tax and non tax revenue. Tax revenue constitutes significant portion in government revenue. In total tax revenue of Nepal, direct tax has greater portion than indirect tax. It is not a good symptom that the portion of direct tax revenue is low and the government is largely depending upon indirect tax. For the economic development of the country, contribution of direct tax is more essential rather than indirect tax. Among the direct tax, income tax plays a vital role. Hence, the following research question will be addressed in the study:

- i) What is the growth trend of tax revenue, direct and indirect tax revenue of Nepal?
- ii) What is the government expenditure coverage by tax revenue in Nepal over the studies period?

1.3 Objective of the Study

The main objective of the study is analyzing the contribution of tax on government revenue. The specific objective of the study is as follows:

- i) To analyze the growth trend of tax revenue, direct and indirect tax revenue of Nepal.
- ii) To examine the government expenditure coverage by tax revenue in Nepal over the study period.

1.4 Significance of the Study

Tax revenue plays a significant role in the overall economic development in developed as well as developing countries. It occupies a very important role in overall government revenue. The role of tax revenue is gradually increasing in the world because of economic betterment of countries.

Nepal is one of the lowest taxed economies in the world as her Tax/ GDP among as well as TAX/GDP ratio is the lowest among SAARC countries and among the rest of the world as well. This shows poor performance of tax management in Nepal. The portion of indirect tax is greater than direct tax. However, it should be just reverse for

economic welfare. The role of income tax should not be minimized in Nepal due to the various problems. It may also be useful instrument to measure the living standard of people. But the tax administration of Nepal is suffering from various problem, the main problems of the administration of Nepal are inappropriate tax policies, administrative bottlenecks of indirect tax structure and existence of mass poverty.

Nepal is least developed country of the world. The resources collected internally are sufficient to run day- to -day administration of the country but the revenue surplus is not adequate to undertake adequate developmental activities. So, the country is heavily dependent on the foreign aids and grants to undertake its development activities. Out of various sources of income tax is an important source for revenue. It is regular sources of tax revenue too. Income tax has been contributing to the tax revenue of Nepal. There are studied about revenue like as VAT, excise duty, so this study is directed acquiring information about tax revenue collection from Inland Revenue. This study might be fruitful for the researcher, tax officers and tax experts.

Again , as being very much important role of tax revenue in economic development to study about tax is needed, because it gives helps the policy makers as the research as supposed to become milestone for them . Though, a big attention has been given towards the subject matter, those are not being sufficient to through the light upon our subject matter.

1.5 Limitations of the Study

Most of the research study is limited by the time period, area of study undertaken and collection of information and data. This research study confined within the following limitation.

- i) Mainly the research relies on secondary data collected from several publications of Ministry of Finance and related websites.
- ii) The sample period of the study is FY 1990/91 – FY 2015/16.
- iii) It focuses on aggregate analysis rather than highly disaggregated ones.
- iv) The analysis is limited to current price figures and does not consider constant price analysis.

1.6 Organization of the Study

The study has been divided in to five chapters which are as follow.

The first chapter includes the general back ground, focus of the study, statement of the problem, objectives of the study, significance of the study, limitations of the study, chapter two contains two parts i.e. conceptual review of the selected topic and review of literature. it again contains the review of literature of previous research on the relevant subject matter. Chapter three explains the research methodology used for the purpose of the study which includes conceptual framework, research design, sources of data, data collection procedure, the conceptual frame work contains the theoretical aspects of tax, tax from different perspective and concept.

Chapter four includes presentation and analysis of data. This chapter growth rate of tax revenue, contribution of tax revenue to government's revenue and expenditure.

Chapter five includes summary, conclusion, recommendations and references have been included at the end of the study.

CHAPTER II

LITERATURE REVIEW

2.1 Introduction

The government of a country requires sufficient revenues to carry out development plans, to handle day-to-day administration, to maintain peace and security and to launch other public welfare activities. In order to carry out such activities, the government collects revenue from different various sources such as tax, remittance, income from public enterprise, special assessment, fees, grant, deficit financing and assistance etc. However across all these sources of collection the public revenue, taxation is the main source since it occupies the most important part of government revenue. Therefore, some people like to say tax is the sinews of the state, for mobilizing various sources of revenue.

There are very few studies which have been conducted on tax revenue as a source of government revenue in Nepal. This chapter refers to review of different books, articles and previous theses done by different persons on taxes. Some of the relevant related studies to the subject matters were reviewed below.

2.2 Theoretical Concept

Meaning of the tax regarding tax is explained in this section. Definition and meaning of taxes by various economists is also explained in this section. Tax refers to the compulsory contribution to the nation by its people for whom the nation provides security to them. Taxes are levied primarily to raise revenue for the government expenditures, although they rise for other purposes as well.

The development country's primary purpose of taxation is the avoidance of inflation; however, it leaves the twin objectives of rapid economic development and narrowing the inequality of income and wealth of developing countries (Chelliah, 1993).

Regarding the role of taxation in developing countries like ours, the thing in sound manner in any country like Nepal where there are no discovered mineral resources for the expansion and diversification of international trade, significant industrial development and agricultural level taxation has a critical role to play in accelerating the pace of economic development (Dahal, 2005).

From the above definition, it can be said that tax is a compulsory levy and those who are taxed have to pay it without getting corresponding benefits. The tax payers don't have any right to receive direct benefit from tax paid. Due to the compulsory trend, people have expressed different views in different ways about the taxation. " No thing is certain in this world but death are taxes " while other says " death means stopping to tax pays" (Kandel, 2006).

The concept of modern tax which is an outcome of western thought contains different fundamental principles, some of them are followings.

- i) No taxation without representation.
- ii) Tax can be levied only with the approval of citizens through their representatives.
- iii) Foreigners are required to pay more tax than citizens.
- iv) When a state levies tax, it is to be collected compulsory and tax payers are compelled to pay as it is their liability.

A government can only impose tax to the natural person and legal person as per the prevailing laws. In the history of tax in Nepal, in Lichhabi period, the main source of revenue of the government was tax. There are tri-karabhaga (tax on agriculture), bhoga (tax on livestock) and kara (tax on trade). Other different taxes were imposed on different areas. Anshubarma, one of the periods of Lichchhabi period imposed water tax and religious monument repair tax. in the malla period , there were tax related to land, trading etc. Jayasthitimalla imposed taxed on cremation (dahasaskar) and caste purity. In Shah period also, there was continuation of tax system of malla period, i.e based on land and trade, after unification, different types of taxes like land tax. Transit tax, forest product tax, mining tax, market duties were levied. In the Rana period, the main sources of government revenue was land tax, customs duties and excies . The tax system was based on contract, amanat ,jimmal, mukhiya and dittha were the persons who used to collect the tax . Sanads and sawals were the law guiding tax system. lagati (based on lagat record) and hansawali (not based on record) were two types of revenues . jammanajodnu ,kachchanachhodnu (not to get total and not to leave even a single paise) was the principle of revenue collection in the rana period.

After the drawn of the democracy, the first budget was introduced in 1952 (2008 B.S). After that so many reforms in tax system are carried out in Nepal. Different types of tax laws such as customs, excise, income tax, sales Tax \VAT, local tax and other were introduce and abolished. For the self – reliant economic system and sound infrastructure, the government should generate sufficient public revenue .To meet the public expenditure, the government collects fund through external and internal sources.

2.3InternationalContext

Ahmad and Ludlow (1889) have identified the alternative tax reform packages on vat for Pakistan keeping the distributional consequences in consideration. They have their own method for the tax reform analysis. In the first step, they describe the existing taxes and then, examine the consequences of tax change (and thus price change) on household, resulting government revenue and also implications for production. They were analyzed, and compared the consequences of different options such as the single rate VAT rates. The reform with equal revenue and the reform with additional revenue as well as the production implications of the tax reform are also considered. The work shows that poor. A value- added tax supplemented with selective excises would have made Pakistan's tax system more buoy and reduced the production distortions inherent in Pakistanis then current tax system and not at the expense of the poor.

Chelliah (1993) has expressed the desirability of full- fledged VAT for India. the committee observed that “ the idea solution, from the economic point of view , to have a single VAT at the central level , reaching down to the retail stage in replacement of most indirect taxes other than protective duties and sumptuary excise duties the central excise , then state sales the taxes the municipal control . The goods and passenger tax and the electricity duty” the Indian budget of various fiscal year indicated the intention of India and introduce a VAT in order to rationalize the commodity tax system.

Gueard (2003) has described analyzed , and evaluated the Brazilian VAT against the background provided by two broader issues : one as a case study of the VAT in a developing country another as an illustration of the problem posed by inter- state tax co- ordination in a special setting of a federation caused by huge regional disparities .

The Brazilian state adopted a broad based single rated (i.e. 15%) VAT in 1976 in the place of existing heterogeneous turnover taxes aimed origin to secure a greater degree of tax co-ordination among the states of the terminations. The VAT was based on modified original principle and it extended to retail with minimum exemptions. The administration of the tax did not appear burdensome. In the first year of its introduction, revenue increased by 54% the 30% of which was due to price increased and 17% was the real income. the industrial sector bore a heavier tax impact than rest of the economy in relation to its own value added because of the non- deductibility of tax on inputs used by the industrial from the exempt sector. Manufacturing accounted for 60% of estimated VAT although it generated less than one fourth of the GDP. The brazilin experiences do suggested that the VAT techniques can be applied to the condition in developing countries with no great difficulty. The administration VAT could be express to pose initially a more difficult problem in developing countries, which previously have no experiences in operating a broad based sales tax. Casanegra - 2003_ has showed about VAT in developing countries and found that at the time when the introduction of VAT was gaining a momentum in developed as well as in developing countries. The study examined (the applicability of VAT in seven developing countries adopted the VAT considering the fact that many uncertainties arise in the introduction of any major new tax especially with which developing countries have very limited experiences. According to the study , the most important feature of VAT in developing countries was its conceptual basis such as taxable base, exemptions treatment of small trade etc. problems of implementing a VAT in developing countries are also great. In fact, the feasibility of VAT in developing countries depends largely upon the ability of those countries to administer it. The administrative efficiency was influenced by the structure of VAT employed and the economy's social and economic development. The problems should also be viewed from the angle of taxpayers compliance, as the cost of doing business tends to increase with VAT because of the need to adopt new accounting procedures. The study showed that VAT produced between 10 to 30% of government revenue of the seven developing countries covered by the study and the VAT revenue in these countries was expected to increase at faster rate than the rate of growth of the economy.

2.4 National Context

Several books, research papers have been reviewed while conducting this study. Many individuals and organizations have made appreciable efforts in the field of income tax, many literatures are found in the field. Most of them are concentrated to administrative problems, legal aspects and policies in the descriptive way rather than analytical. Review of available materials based on income tax is certainly helpful to the subject matter in the contribution of tax revenue of Nepal. For this purpose, literature has been reviewed as:

Lent (1968) has critically analyzed the scope of income tax, taxable income, exemption and allowances. His findings showed " Nepal would appear to have few pre-requisites for the successful implementation of an income tax." he suggested income tax and contribute much more if necessary reforms are undertaken both in income tax law and in its administration. Analysis the income tax rate for structure for individual and company, he suggested that increment in person's income tax rate at lower taxable income and reduction of rate at intermediate income bracket are desirable because this will induce people to invest more. For period, the income tax concessions given to industries were not desirable for him then he suggested to lowering the year. Though this study is helpful for improving income tax but cannot be regard in a complete one because in this study emphasis given more for redrafting of law.

Agrawal (1980) has described the different concepts of income tax. He has described the resources mobilization through income tax, fiscal policy, role of income tax, legal provisions relating to income tax, administration aspect of income etc. various mathematical calculation had been shown such as per capita income, buoyancy and coefficient of income tax, elasticity and coefficient of income tax etc.

Khadka(2002) has concluded that the governments expands its expenditure which always exceeds the sources of financing. Budget implementation was poor and targeted program were not fulfill timely. Government has financed the deficit from external loans and internal borrowing instead of internal sources mobilization with strong financial discipline. The portion of development expenditure was slightly higher than regular expenditure in the initial years. But in the later years regular expenditure exceeds development expenditure reflect poor scenario of the economy.

In the reference period, budget did not have significant program to reducing poverty, inequality and increase the living standard of lower classes.

He has identified the major problems of income tax system as inefficiency of tax administration and tax evasion. He observed that the tax authorities were insufficient to enforcement of law. There were no integrated program for taxpayer's education, assistance, guidance, and counseling. Tax office was looked upon as heaven for corruption. Insufficiency, delays, unfair dealing, harassment and incompetent personal were the major problems of tax administration. He further added," it is increasingly being felt that the potential of income tax in Nepal has been very much under realized and reforms are urgently needed in this tax. In Nepal income tax efforts have been constrained by hastily formulated policies, ambition law, poor coverage, poor enforcement as well as compliance and bad image of tax administration. its potential has been remained underutilized. A comprehensive study for reform of income tax in Nepal therefore has become necessary.

Kayastha (2003) has analyzed the problem and prospects of resources mobilization through direct taxation in Nepal. In this context, he has analyzed that tax structure (during 1994 to 2001) and responsiveness of major tax (during 1994/95 to 2001/02). He has found that elasticity of tax in Nepal was extremely low (0.59) in comparison with buoyancy for total revenue as well as individual taxes (1.47). These finding indicate that the government has concentrated more on introducing various discretionary measures rather than broadening the tax base, which was not favorable to support growing development activities.

Nepal (2005) has concluded that the major problems existing in Nepalese tax system are the inefficient income tax administration, mass poverty, lack of tax consciousness, low number of tax payers, lack of co-operation between taxpayers and department, narrow coverage, assessment deficiency etc. Problem can be solved and resources are efficiently utilized, the future income of income tax would be bright. The exemption limit should be separated to couple and family and tax rate would be bright. The exemption limit should be separated to couple and family and tax revenue and tax rate and exemption limit should be elastic, scientific and progressive.

Pant (2006) has tried to show the income tax system and its role on national economy. The study concluded that there is problem of lack of effective personnel management,

reward and punishment system, lack of managerial efficiency, poor income tax assessment procedure, poor tax information system and lack of tax payer's education, very narrow coverage of income tax.

Suwal (2008) has concluded that the increasing magnitude of resource gap clearly indicates that there is an urgent need of mobilizing additional resources. Income tax as appeared one of the most effective fiscal policy instruments to mobilize additional resources and achieving the desired development objectives of Nepal. Income tax is a composition of income tax from public enterprise bodies, income tax from individual, income tax from remuneration and tax on interest. Definition income is vague, low paying capacity of tax patters, lack of tax consciousness in tax payers, higher tax rate and corruption.

Aryal (2011) has studies," The trend of different source of taxation shows that the contribution of total tax revenue from direct taxes has continuously declined and indirect taxes have continuously risen. The trend shows that magnitude as well as percentage contribution of traditional direct taxes i.e. lands tax decline continuously, oppositely income tax and registration duty are growing. High tax revenue contributor sector i.e. customs duties also are in the first position presently. However, the revenue from import duties has set at second position. It has substituted by sales tax. Excise duty is also increasing trend. Therefore, Nepalese tax revenue is heavily reliant on in directed taxes.

According to this study, elasticity and buoyancy coefficient of overall taxes were less than unity. It meant that it was inelastic in trend. The export duty had negative elasticity. In fact, the inelastic trend of tax system in developing countries were an inheritance characteristic resulting from heavy reliance in indirect taxes. The share of indirect taxes was around 70.5% and non-tax revenue is 6.9% on total revenue.

Shrestha (2010) has concluded that revenue collection from income tax was low. Income tax law has inappropriate and the administration was worse. She suggested that the income tax laws and administration in Nepal should be deeply scrutinized and properly implemented, strong commitment, fair and uniform imposition were stored. Human resources development planning within the administration was desired for the efficiency of tax personnel side by side. Tax education package should be made and initiated.

Poudel (2011) has concluded that the reform of tax administration, successful implementation of VAT and establishment of standardize accounting system was necessary. Total revenue was dominated by tax revenue which is 78.2% and nontax revenue was only 21.9%. Tax revenue was increasing in recent days and non- tax revenue decreasing trend.

Lamsal (2011) has concluded that the income tax administration of Nepal was not efficient enough due to lack of trained employees, less consciousness of taxpayers, lack of income tax experts/professional in tax administration, defective income tax act, increasing habit of tax evasion etc. The tax laws should be reviewed and reformed, expertise and professionalism should be increased in tax administration and tax education should be provided to taxpayers on regular basis.

Luitel(2012) has concluded that the contribution of income tax to GDP was very low in comparison with other-developing countries. There was weak policy and commitments to collect revenue through income tax. Definition of income was ambiguous and it should be modernized and simplified.

Dahal (2012) has mentioned that the subject of taxation had undergone an extensive metamorphosis since last many years. With the advent of supply side the role of taxation has become even more crucial. Taxation is not only an effective instrument for resources mobilization-a 'bot-strap operation for financing economic development-but also a 'took-tik' for revenue collection to sustain growth and maintain equity and stability in the economy. If blood circulation is desirable to keep the human body alive so is taxation to keep the economy alive. The laws of blood circulation and taxes are tantamount to each other. In developing economies the resources gap is critical and widening resulting to huge fiscal and budgetary deficits. The growing resources gap is frequently off-set by mobilizing internal and external borrowing and consequently shifting the burden of debt to posterity. Therefore, revenue mobilization is a challenging proposition in developing economies where a majority of the people lives in abject poverty and the people engaged in economic activities have extremely limited taxable capacity. In addition, legal base of taxation is compressed with unlimited tax shelters and tax administration lacks innovative mechanism to identify new tax payers and bring them into tax-net, In developing economies, unsanctioned economic activities have greatly increased over the year resulting to poor voluntary compliance due to indifferent attitude of the taxpayers toward government spending,

Thus, interface between diminishing efficiency of tax administration and delinquency on the part of taxpayers is becoming critical.

The writer has mentioned that according to 'theory of tax structure change during economic development' the share of direct taxes will increase with rise in per capita income, while the contribution of indirect taxes subsequently declines. Excessive dependence on customs duties is manifestation of backward economy characterized by predominance of underemployment in formal sector. Direct taxes have strategic significance and its superiority is claimed over indirect taxes on the ground of neutrality, welfare and excess burden. The Hicks-Joseph proposition of excess burden established superiority of direct taxes over indirect taxes, for direct taxes do not cause a reorganization of consumer's choice which is not dictated by changes in the cost of production. A high level of sustainable economic development is always coupled with increasing contribution of direct taxes to the tax structure. The role of indirect taxes becomes prominent after the dis-solution of traditional society. The international comparison of taxation showed that average Tax/GDP ratio in OECD countries found to be 36.3% in 2004, while it was 50.7% in Sweden, 50.6% in Denmark, 30.6% in Belgium, 35.1% in New Zealand, 29.6% in USA, 27.1% in Japan, 24.6% in South Korea, 18.5% in Mexico, 16% in India, 12.9% in Pakistan and around 12% in Nepal during the same period. It is estimated to be 18.4% in FY 2015/16.

2.5 Research Gap

Various literature in international suggest that the role of government is vital for the economic growth. In case of Nepal lots of work has been conducted indeed. Though there is still numerous unaddressed issues on government taxes. To fill the gap about the government taxes this research might be a brick to give support on its foundation.

CHAPTER III

RESEARCH METHODOLOGY

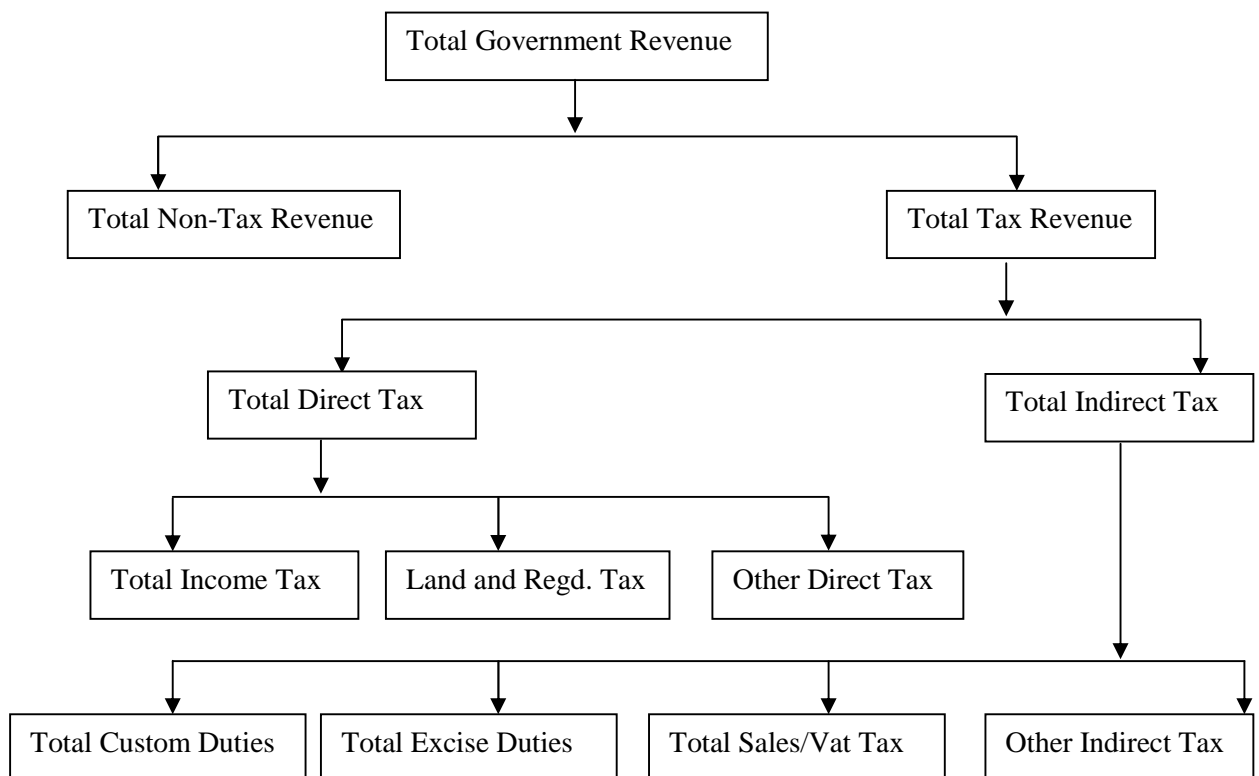
In this chapter we present the conceptual framework of the study, research design, and sources of data and method of data analysis. The study is based upon secondary data to fulfill the objective of the study. The secondary data and information were collected from different sources such as budget speech of various year, statistical abstracts, ministry of finance, economic survey of Nepal government, publication of world bank, united nations and NRB various periodic plan of Nepal, government finance statistical year book, etc.

3.1 Conceptual Framework

Excluding foreign aid, tax is the main income source of government revenue. For self-reliance in economic growth of the economy, the government has to extend significantly the domestic and international tax value generating the various resources and increase the per capita income of the people for the developing countries. The conceptual framework of this study is outlined in figure 3.1

Figure 3.1

Conceptual Framework



In the early days the budget was sharply confined to two objectives, such that first government had to determine how much money it needs to take out of pocket of the tax payers in order to maintain its necessary activities and secondly, the legislature role of government towards a welfare state its responsibility has been wider. In such circumstance the budget has wide spread ramification though out the national economy, because the size of the budget to affect the rest of the economy has been greatly enhanced (Gupta, 1967).

The revenue of government comes from basically two source tax and nontax. Non-tax revenue includes different sources like duties and fees, fines, public utilities, dividends, and Interest etc. The administrative income denotes the amount charged by the government for providing administrative services such as registration fees, passport fees, tourism fees, and other fees, fines and penalties, forfeiture etc. other components of Non- tax revenue are forest postal services, dividends, interest, royalty, sales of government property etc. Another source of government revenue is the taxation like custom duty, excise duty, value added tax, corporate and personal income taxes. These are the major components of tax revenue. For a tax planner, one person should know the meaning and certain provisions related to all these taxes. The falling is certain taxes which the business community should encounter tax during day- to-day business life and which provide mast of the revenue of Nepal Government.

A tax imposed on income base is called income tax. Income tax is divided into two parts- individual income tax and corporate income tax. Income tax to be paid by individual or couple or sole proprietorship firm is individual income tax whereas income tax to be paid by entity is called corporate income tax. The marginal tax is 25% for an individual and 20% for an industry, 30% for financial institution and 25% for a corporate body. Income tax, as the word itself refers to a tax levied on income. In a board sense, income tax is a levy based upon the receipt or gain of the taxpayers within a definite period of time. From the beginning, income tax has always been regarded as s tax based on the cannon of ability. The tax could be adjusted as to exempt the lowest income groups from the operation of the tax and make the richer groups bear the burden of the tax according to their apart from such consideration as revenue productively. Different countries may have different concept on income tax.

In Nepal, income tax is levied on the net income derived after deducting all allowable deductions.

Taxes imposed by a country on import and export of goods when the goods cross the boundaries of the country are called customs duty. Since this tax is levied on goods traded between two nations. It is also called border tax. Customs duty has basically two objectives: collecting revenue and regulating the international trade. Customs duty can be divided into two parts: import duty and export duty. The customs rates for import duty are composed of 5%, 10%, 15%, 25%, 40% and 80% whereas customs rates for export are 0.75%, 1.5%, 2%, 4.5%, 10%, 70%, and 200%. The 200% rate is imposed on export of forest wood. Certain items are exempted both from import duty and export duty.

Value added tax is the developed from sales, tax. The basic objective of value added tax is to collect revenue. It is the tax imposed on the value addition in each stage of production or sales. The rate of value added taxes in Nepal are 0% and 13% certain goods and exempted from value added tax. Threshold amount of transaction registering for this tax purpose is Rs 20 lakhs.

Taxes levied on manufacture, sale or consumption of goods or services injurious to health or luxurious goods is called excise duty. Previously, it was confined only on national goods. However, in these days, excise duty is levied on imported goods also. This tax is imposed with some objective like collecting revenue, controlling the consumption of injurious and luxurious goods and sometimes for redistribution purpose. Local tax is the tax imposed by local governments. IT groups of taxes such as property tax, vichel tax, business tax, etc.

3.2 Research Design

This research study follows the descriptive research design. Secondary data will be collected from various sources. Data will represent in the table and graph. The growth trend and expenditure coverage by revenue will be used as an instrument for the analysis research objectives.

3.3 Nature and Sources of Data

To achieve the main objectives of this study, secondary sources of data and information will be collected. The collection will be done in accordance with the

ability and usefulness of this study. The sources of data used in the study are as follows.

The secondary sources of data were the information received from reports and related websites etc. the major sources of secondary data are as follows.

- i) Annual reports of income revenue department, ministry of finance, government of Nepal.
- ii) Published documents and quarterly economic report of Nepal rastra bank.
- iii) Economic surveys and budget speeches, ministry of finance.
- iv) Books, thesis and relating to tax administration available at the central library of T.U
- v) Publications of centre for economic development and administration (CEDA), T.U
- vi) Different publications of central bureau of statistics.

3.4 Procedures of Data Collection

Collective data of various sources are firstly tabulated into separate format in systematic manner. The data are tabulated into various tables according to the subject in order. Then they have been presented and analyzed in descriptive way. Graphs and charts are also presented to interpret visually the findings of the study. Mainly the secondary data are collected reports, related websites, and annual reports of IRD, MOF and NRB.

3.5 Methods of Data Analysis

According to the subject matter and requirements, the data were tabulated into separate etc have been used. The data has been presented and analyzed in the descriptive way. Graphs and charts have also presented to interpret visually the findings of the research study. To make the study more analytical and precise the growth trend of tax revenue, government revenue with grant and without grants and expenditure are calculated from of time series data for the period 1990/91 to 2015/2016.

CHAPTER IV

PRESENTATION AND ANALYSIS OF DATA

This chapter is the main part of the study because in this chapter collected data are presented and analyzed with the help of various tables, graphs etc. This chapter is performed to show the clear picture of the contribution of the tax revenue and non tax revenue to the government's total revenue.

4.1 Growth Trend of Tax Revenue

Tax revenue comprises customs, tax on consumption and product of goods and services. Tax revenue is the main source of government revenue. Table 4.1 shows the growth trend of tax revenue by analyzing of over the period of FY 1990/91-2015/16. The pattern of total tax revenue from FY 1990/91 to FY 2015/16 is increasing. Total tax revenue of Nepal is composed of direct tax and indirect tax revenue. Growth rate of total tax revenue over the last two decade was not consistent.

The highest growth rate was 37.47 % in FY 2008/09 and the lowest was 1.20 % in FY 2001/02. Although the growth rate of total tax revenue increased from 12.25 % to 20.78 % in FY 1990/91 and 1991/92. Total tax revenue decreased by 18.09 % in FY 1992/93 in comparison to FY 1991/92 and in FY 1993/94 grew by 31.80 % while its growth rate began declining and stood at 27.90 % in last two fiscal year, 2014/15 and 2015/16 it was grew up by 13.93 % and 19.96 %. It is necessary to achieve higher and sustainable revenue growth rate for country's rapid economic development. In a situation whereby annual growth rate average for the past 25 years has been a mere 17.23% between FY 1990/91 and 2015/16.

Table 4.1
Growth of Total Tax Revenue (at current prices)

Fiscal Year	Growth of Total Tax Revenue (%)
1990/91	12.25
1991/92	20.78
1992/93	18.09
1993/94	31.80
1994/95	27.90
1995/96	10.21
1996/97	12.72
1997/98	6.15
1998/99	10.90
1999/00	15.29
2000/01	17.25
2001/02	1.20
2002/03	8.28
2003/04	13.12
2004/05	12.31
2005/06	6.14
2006/07	23.93
2007/08	19.64
2008/09	37.47
2009/10	36.51
2010/11	10.92
2011/12	19.46
2012/13	22.60
2013/14	20.37
2014/15	13.93
2015/16	19.96
Average	17.227

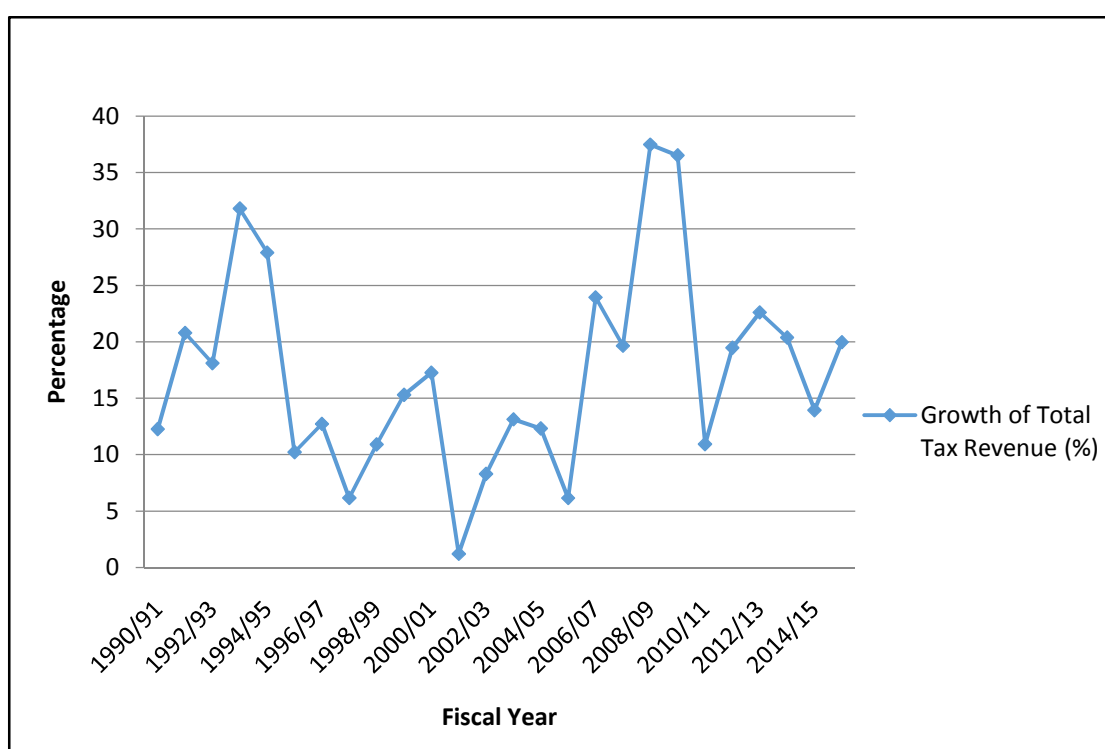
Source: Economic Survey (FY 2015/16) and Quarterly Economic Report(2015/16).

Table 4.1 shows the growth trend of tax revenue on total government revenue of Nepal from FY 1990/91 to FY 2015/16. The contribution of direct and indirect taxes

on total revenue collection of government of Nepal is different. Total government revenue includes total tax revenue and non-tax revenue. Total tax revenue comes to the form of direct tax and indirect tax so on. There is some scope for generating more revenue through the rationalization of tax source particularly by improving government policies and operational performance.

The growth trend of total tax revenue of the government of Nepal over the period of 1990/91-2015/16 is depicted in Figure 4.1.

Figure 4.1
Growth of Total Tax Revenue (at current price)



Source: Economic Survey, 2015/16

By analyzing figure 4.1 shows the growth rate of total tax revenue are ups and down trend in overall period, where 37.47% is the highest growth rate in FY 2008/09 and 1.20% is the lowest growth rate in FY 2001/02. The average growth rate is 17.227%. According to the above graph the growth trend of tax revenue is volatile.

4.1.1 Growth Trend of Direct Tax

In Nepal's tax structure, the main components of direct tax are income tax and land registration taxes. Table 4.2 shows that the growth trend of direct tax revenue of Nepal from FY 1990/91 to FY 2015/16.

Table 4.2
Growth Trend of Direct Tax (At Current Prices)

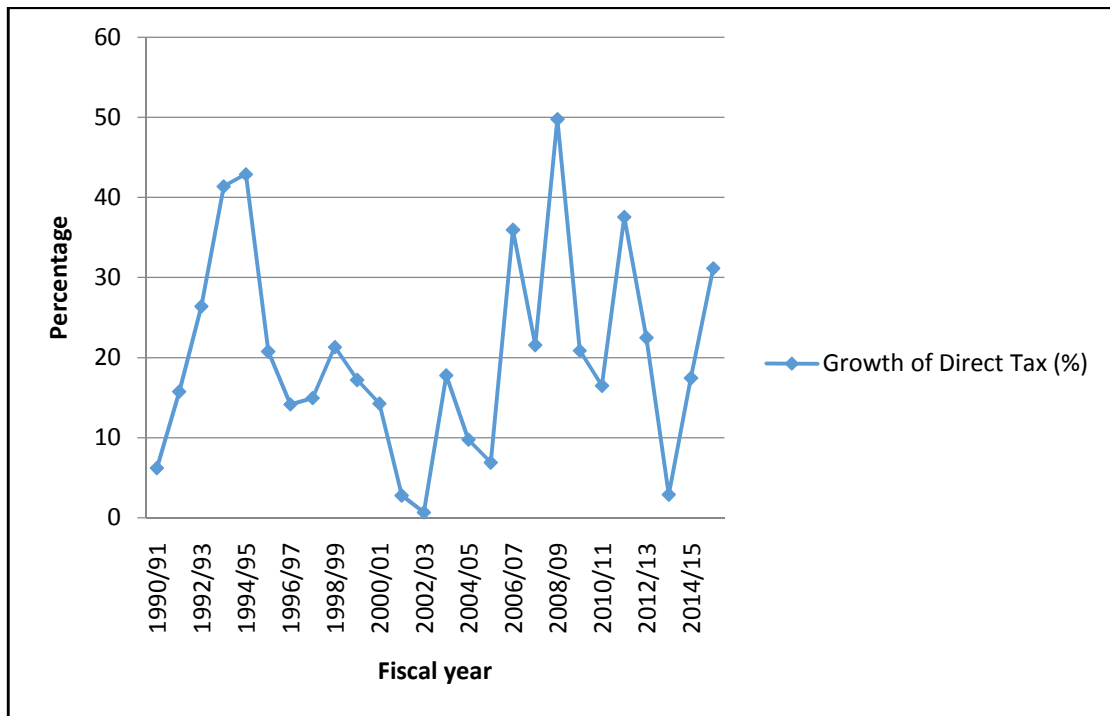
Fiscal Year	Growth of Direct Tax (%)
1990/91	-6.19
1991/92	15.74
1992/93	26.38
1993/94	41.37
1994/95	42.88
1995/96	20.76
1996/97	14.14
1997/98	14.94
1998/99	21.30
1999/00	17.19
2000/01	14.25
2001/02	2.76
2002/03	0.66
2003/04	17.77
2004/05	9.74
2005/06	6.89
2006/07	35.94
2007/08	21.56
2008/09	49.77
2009/10	20.86
2010/11	16.48
2011/12	37.55
2012/13	22.47
2013/14	2.87
2014/15	17.43
2015/16	31.14
Average	19.50

Source: Economic Survey (FY 2015/16) and Quarterly Economic Report (FY 2015/16).

Table 4.2 shows that the growth trend of direct tax revenue of Nepal from FY 1990/91 to FY 2015/16. Total direct tax revenue of Nepal is composed of income tax, property tax and other tax revenue. Growth trend of direct tax revenue over the last two decade has not been satisfactory. The highest growth rate was 49.77% in FY 2008/09 and the lowest is -6.19% in FY 2001/02. The growth trend of direct tax is 19.50% from FY 1990/91 and 2015/16.

The growth trend of direct tax revenue of the government of Nepal over the period of 1990/91-2015/16 is depicted in Figure 4.2.

Figure 4.2
Growth Trend of Direct Tax (At Current Prices)



Source: Table 4.2

By analyzing figure 4.2 shows the growth trend of direct tax revenue are highly up and down trend in overall period. The fiscal year 2008/09 is the greatest and fiscal year 1990/91 is the lowest growth trend than that other fiscal year. The average growth rate is 19.50%. According to the above graph the growth trend of direct tax revenue shows highly fluctuating trend.

4.1.1.1 Growth Trend of Income and Other Taxes

In Nepal's tax structure, the main components of direct tax are income tax and land registration taxes. Table 4.3 shows that the growth trend of income tax and land registration taxes of Nepal FY 1990/91 to FY 2015/16.

Table 4.3
Growth Trend of Income and Other Taxes (at current prices)

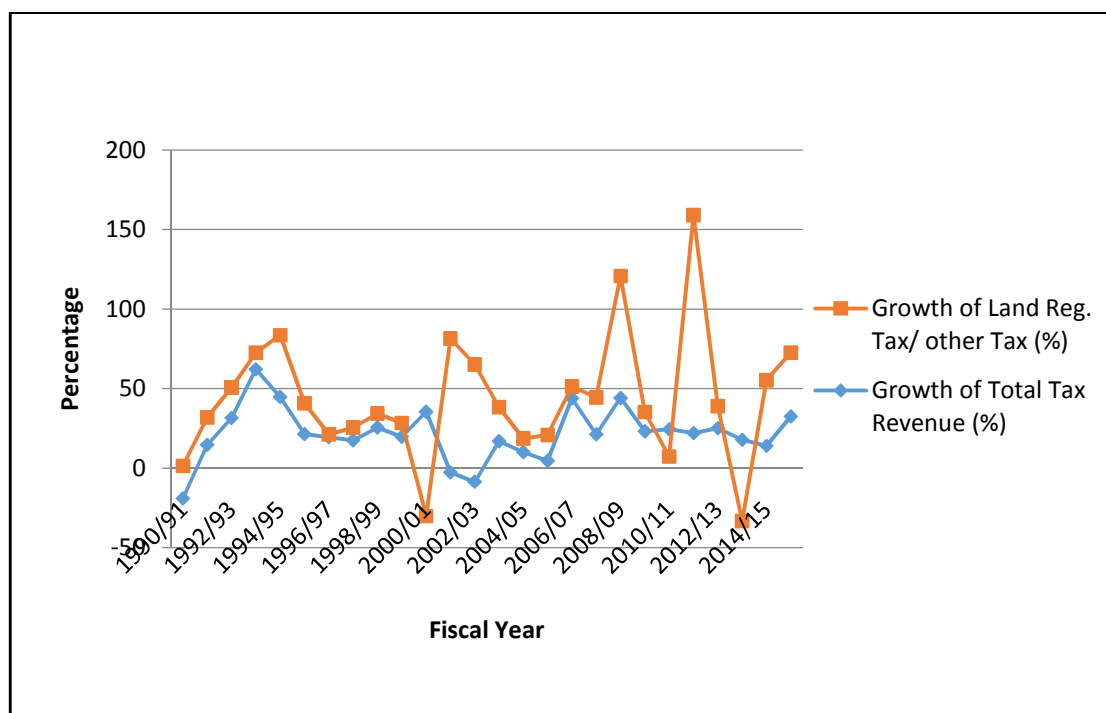
Fiscal Year	Growth of Total Tax Revenue (%)	Growth of Other Tax (%)
1990/91	-19.15	20.56
1991/92	14.59	17.33
1992/93	31.54	19.14
1993/94	62.19	10.36
1994/95	44.75	38.81
1995/96	21.39	19.32
1996/97	19.47	1.77
1997/98	17.49	7.98
1998/99	25.51	8.84
1999/00	19.67	8.71
2000/01	35.46	-65.63
2001/02	-2.73	84.19
2002/03	-8.66	73.78
2003/04	16.87	21.50
2004/05	10.02	8.65
2005/06	4.57	16.22
2006/07	43.87	7.32
2007/08	21.22	23.19
2008/09	44.12	76.68
2009/10	23.12	12.10
2010/11	24.34	-17.08
2011/12	21.98	137.17
2012/13	25.07	13.90
2013/14	17.81	-51.13
2014/15	13.96	41.30
2015/16	32.50	40.01
Average	21.58	22.12

Source: Economic Survey (FY 2015/16) and Quarterly Economic Report (FY 2015/16).

Income tax and land reg. land other tax are important source of direct tax. From table 4.3, it reflects that the income tax has increased highly 62.19% in FY 2093/94 as compared with other fiscal year. The lowest growth is -19.15% in FY 1990/91 and average growth is 21.44%. The highest growth of land and reg. tax and other tax is

137.17% in FY 2011/12. The lowest growth is -65.73% in FY 2000/01. The average growth rate is 20.58%. But the growth rate of last two fiscal year is good. From the table, the growth trend of income tax and other tax including land registration taxes, is fluctuating ups and down.

Figure 4.3
Growth Trend of Income and Other Tax (at current prices)



Source: Table 4.3

From the above figure, it shows the growth trend of land and reg. /other tax is more fluctuating compare to income tax. There are so many up and down fluctuating situation in overall period. The lowest growth is -19.15% in FY 1990/91 and average growth is 21.44%. The highest growth of land and reg. tax and other tax is 137.17% in FY 2011/12. The lowest growth is -65.73% in FY 2000/01. The average growth rate is 21.58%.

4.1.2 Growth Trend of Indirect Tax

The indirect tax in this study refers to three categories of taxes: Customs duties VAT and Excise duties, the growth trend of indirect tax shown in Table 4.4.

Table 4.4
Growth Rate of Indirect Taxes (at current prices)

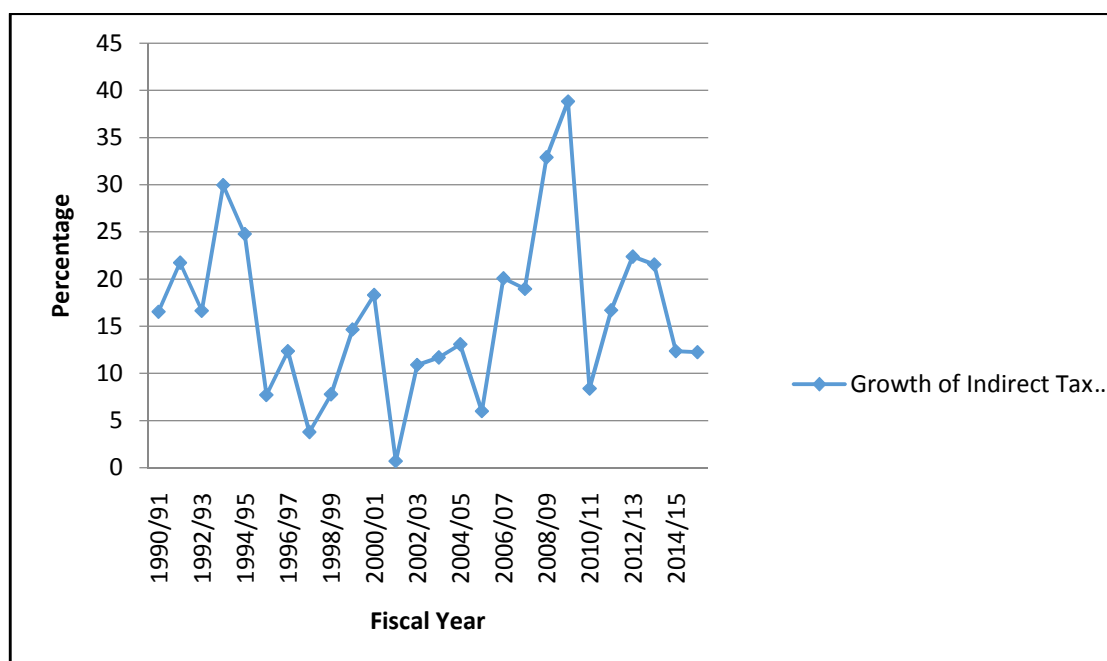
Fiscal Year	Growth of Indirect Tax (%)
1990/91	16.52
1991/92	21.72
1992/93	16.62
1993/94	29.96
1994/95	24.77
1995/96	7.69
1996/97	12.34
1997/98	3.76
1998/99	7.76
1999/00	14.64
2000/01	18.29
2001/02	0.68
2002/03	10.88
2003/04	11.68
2004/05	13.07
2005/06	5.98
2006/07	20.07
2007/08	18.95
2008/09	32.90
2009/10	38.83
2010/11	8.37
2011/12	16.68
2012/13	22.37
2013/14	21.54
2014/15	12.34
2015/16	12.23
Average	16.18

Source: Economic Survey (FY 2015/16) and Quarterly Economic Report (FY 2015/16).

Table 4.4 shows the growth trend of indirect tax. There is no any negative growth trend in indirect tax because the improvement in VAT implementation is the main reason for such a satisfactory performance. The highest growth rate is 38.83% in FY

2009/10 and the lowest growth rate is 0.68% in FY 2001/02. The average growth rate is 16.18% in overall study period. According to the table, growth rate of last two year's (2014/15 and 2015/16) growth is consistent, though the rate is below average. The growth trend of indirect tax of the government of Nepal over the period of 1990/91-2015/16 is also depicted in Figure 4.4.

Figure 4.4
Growth Trend of Indirect Tax (At Current Prices)



Source: Table 4.4

By analyzing the figure 4.4 it shows the growth trend of indirect tax revenue fluctuated over the given time period. It is observed that 38.83% is the highest growth rate in FY 2009/10 and 0.60% is the lowest growth rate in FY 2000/01. The average growth rate is 16.18%. According to the above graph, the growth trend of tax revenue shows the ups and down trend and it ranges in between zero to around 40 %.

4.1.2.1 Growth Trend of Custom Duties, Excuse Duties and Sales/VAT

The indirect tax in this study refers to three categories of taxes viz. Customs duties, VAT and Excise duties. The growth trend of these indirect tax are shown in Table 4.5.

Table 4.5**Growth Trend of Custom Duties, Excise Duties and Sales/VAT**

Fiscal Year	Growth of Custom Duties (%)	Growth of Excise Duties (%)	Growth of Sales Tax/VAT (%)
1990/91	13.39	11.97	22.88
1991/92	10.33	18.25	44.73
1992/93	17.45	2.35	21.25
1993/94	33.21	9.62	36.49
1994/95	33.54	4.09	28.65
1995/96	4.41	17.40	6.52
1996/97	13.40	18.31	10.80
1997/98	2.30	25.39	-0.25
1998/99	11.97	2.29	10.89
1999/00	13.61	6.10	24.96
2000/01	15.40	21.45	25.70
2001/02	0.11	4.43	-0.93
2002/03	13.96	20.24	9.78
2003/04	9.26	30.22	7.65
2004/05	0.95	3.61	30.35
2005/06	-2.28	0.93	14.38
2006/07	8.83	43.60	20.96
2007/08	26.13	20.18	13.92
2008/09	26.40	44.91	32.97
2009/10	32.04	49.42	38.61
2010/11	1.58	9.16	12.32
2011/12	21.53	13.99	14.61
2012/13	31.15	19.79	18.00
2013/14	19.44	25.29	21.25
2014/15	10.10	17.90	11.28
2015/16	9.81	22.84	8.71
Average	14.54	17.84	18.71

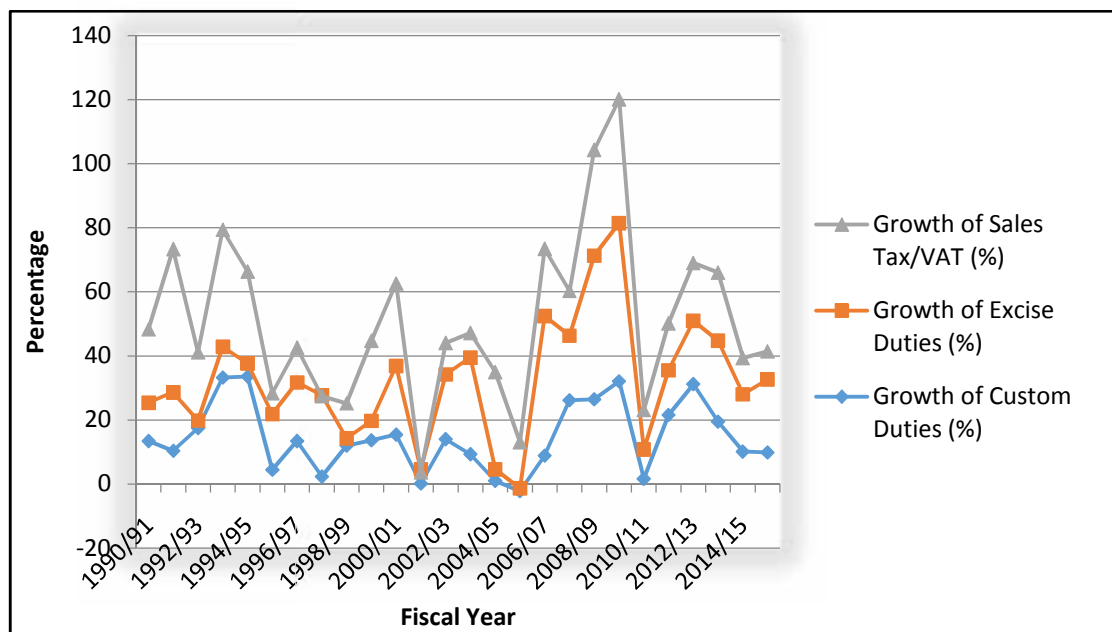
Source: Source: Economic Survey (FY 2015/16) and Quarterly Economic Report (FY 2015/16).

Table 4.5 shows the growth trend of custom duties, excise duties and sales/VAT. The average growth rate of custom duties is 14.54%. The growth trend of custom duties is

in fluctuating trend. The average growth rate of excise duties is 17.84%. The growth trend of custom duties is in fluctuating trend. They average growth rate of sales/AVT is 18.71%. The growth trend of custom duties is in fluctuating trend. Growth rate of different indirect of the last two fiscal year is below average, which indicates the poor performance of taxes collection in Nepal. This is because government is unable to increase the tax base, though is unable to increase the tax rate.

The growth trend of indirect tax of the government of Nepal over the period of 1990/91-2015/16 is also depicted in Figure 4.5.

Figure 4.5
Growth Trend of Custom Duties, Excise Duties and Sales/VAT



Source: Table 4.5

By analyzing figure 4.5 shows the growth trend of all composition of indirect tax revenue are ups and down trend in overall period, where 19.44% is the highest growth rate among all composition. According to the above graph the growth trend of VAT is higher and the growth rate of custom duties are lower. Figure 4.5 also shows that VAT has high fluctuation over the past year due to the conversion of most of the other taxes into VAT.

4.2 Government Revenue and Expenditure

To meet the requirement for day to day administration and development financing, the government collects revenue through various sources. The principal among them are tax and non-tax revenue sources. But limited growth of economy with low level of

income as well as the low rate of saving in Nepal makes exercise of collection tax revenue is insufficient for government expenditure. Besides, high taxation often adversely affects the private enterprises and contributes to a decline in the investment capacity and thereby in employment of the economy.

For developing country like Nepal, the problems of development are enormous and complex in trend. A government needs income for the performance of a variety of functions and meeting its expenditure. It includes all the income and receipt, irrespective of their sources and trend, which the government happens to obtain during any period of time. In the narrow sense, it includes only those sources of income of the government which are described as revenue sources.

So, it is widely recognized that government revenue is the major sources for financing the public expenditure of developing countries. Nepal has also realized this fact. Therefore Nepal has been making constant effort to increase the revenue in their every budget. The public revenue in Nepal has been increasing continuously but only marginal growth has been evident.

Government expenditure means the actual expenditure of government during the specified fiscal year. It can be divided into the following headings.

- i) Recurrent expenditure
- ii) Capital expenditure
- iii) Principal repayment

It is noted that the terminologies used for recurrent and capital expenditure were regular and development expenditure until 2003/04. Current expenditure, Capital expenditure and principal repayment are used to describe government expenditure from 2004/05.

i) Recurrent Expenditure

Recurrent expenditure is one of the major component of total expenditure which is the current expenses. Recurrent expenditure is made up of various components, its main components are expenditure on general administration, social services, defense, economic services, loan, principal payment and interest payment etc. under the heading of miscellaneous other smaller components are included.

ii) Capital Expenditure

Capital expenditure is the public investment and desirable also from the development perspective. This category is of particular importance for the developing economies like Nepal. Capital expenditure is also made up of different components. Its main components are economic services, communication and electricity etc.

iii) Principal Repayment

Principal repayment is the share of internal loan payment and external loan payment. Its share is nominal while comparing with the whole budget. But repayment in principal in Nepal is in gradually increasing trend. External loan depend on foreign exchange rate. Hence, it becomes cheaper when our currency is evaluated and expensive when our currency is devaluated.

Nepal is being a developing country; there is an urgent need of expanding development expenditure, however, there is also growing compulsion to maintain law and order as well as debt servicing. Financing expenditure require increment in revenue collection. Situation of revenue receipts determines the amount necessary for foreign assistance and internal borrowing. The growth of government expenditure in Nepal has been phenomenal as evident from the fact of every finance minister ever since the beginning of the budgeting system in 1951 has presented a public expenditure program larger than that of the previous year (Adhikari, 2005).

4.2.1 Growth Trend of Government's Revenue and Expenditure

The growth trend of expenditure, government revenue with grants and without grants is shown in Table 4.6.

Table 4.6 shows the growth trend of expenditure is ups and down trend in overall study period. The highest growth rate is 36.41% in 2008/09. The lowest growth rate is 0.30% in 2001/02. The average growth rate is 13.78%. The growth trend of expenditure is 19.73%, 16.96%, 19.16% and 20.46% in FY 1990/91, 1992/93, 1995/96 and 2000/01 respectively. There is 20.48%, 20.77%, 18.22%, 14.83%, 14.30% and 54.16% in FY 2006/07, 2007/08, 2009/10, 2011/12, 2013/14, and 2015/16 respectively. The lowest growth rate is 8.74%, 8.98%, 6.17%, 4.91%, 6.47%, 8.12% and 5.74% in FY 1993/94, 1996/97, 1998/99, 2002/03, 2003/04, 2005/06 and 2012/13 respectively.

The lowest growth rate of government revenue with grants is 2.67%, 1.60% and 5.44% in FY 2001/02, 2005/06 and 1997/98 respectively. The highest growth rate of government revenue with grants is 24.97%, 21.75%, 22.22%, 32.78% and 18.37% in

FY 1992/93, 1994/95, 2007/08, 2009/10 and 2012/13 respectively. The average growth rate is 201.17%. The table 4.6 show the overall growth trend is ups and down trend.

The lowest growth rate of government revenue without grants is 8.89%, 8.44%, 3.17%, 3.08% and 11.04% in FY 1996/97, 1997/98, 2001/02, 2005/06 and 2010/11 respectively. The highest growth rate of government revenue without grants is 25.94%, 29.26%, 25.51%, 33.31%, 25.42% and 20.59% in FY 1991/92, 1993/94, 1994/95, 2008/09, 2009/10 and 2013/14 respectively. The average growth rate is 52.38%. The table 4.6 show the overall growth trend is ups and down trend.

Table 4.6

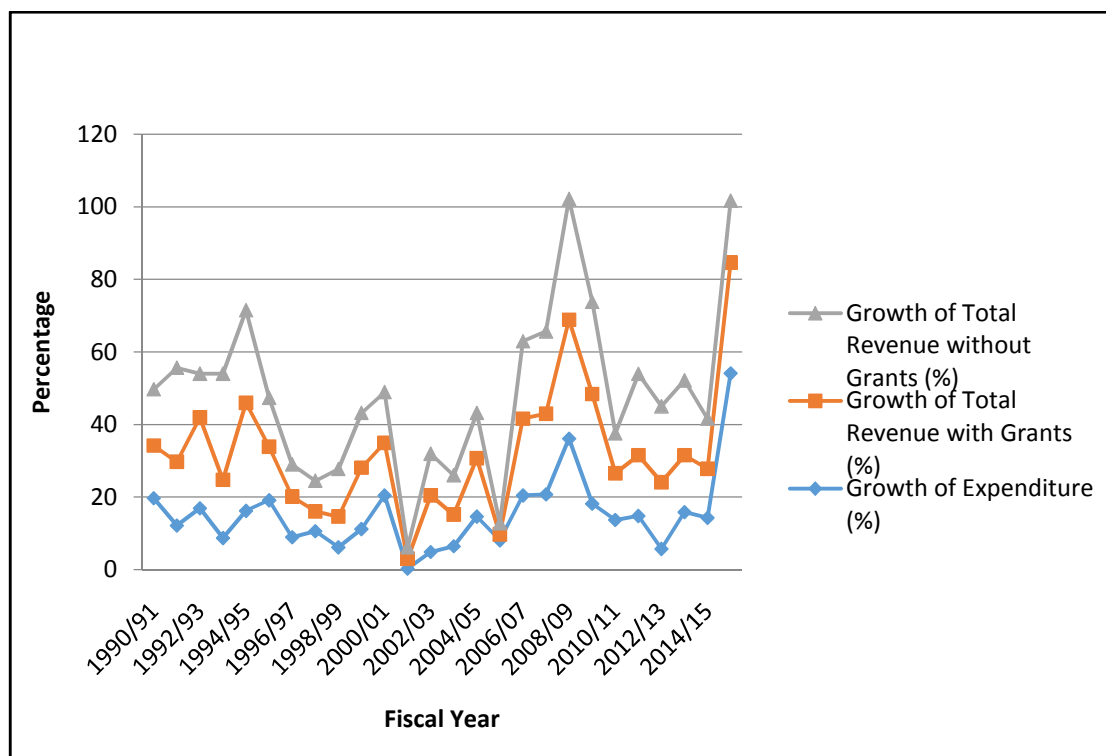
Growth Trend of Government's Revenue and Expenditure (at current prices)

Fiscal Year	Growth of Expenditure (%)	Growth of Total Revenue with Grants (%)	Growth of Total Revenue without Grants (%)
1990/91	19.73	14.48	15.52
1991/92	12.18	17.54	25.94
1992/93	16.96	24.97	12.10
1993/94	8.74	16.01	29.26
1994/95	16.26	29.75	25.51
1995/96	19.16	14.75	13.50
1996/97	8.98	11.14	8.89
1997/98	10.64	5.44	8.44
1998/99	6.17	8.47	13.09
1999/00	11.23	16.87	15.14
2000/01	20.46	14.49	14.00
2001/02	0.30	2.67	3.17
2002/03	4.91	15.57	11.47
2003/04	6.47	8.69	10.85
2004/05	14.67	16.03	12.50
2005/06	8.12	1.60	3.08
2006/07	20.48	21.15	21.35
2007/08	20.77	22.22	22.70
2008/09	36.14	32.78	33.31
2009/10	18.22	30.19	25.42
2010/11	13.74	12.82	11.04
2011/12	14.83	16.74	22.39
2012/13	5.74	18.37	20.92
2013/14	15.87	15.70	20.59
2014/15	14.30	13.49	13.81
2015/16	54.16	30.53	17.04
Average	99.51	201.17	52.38

Source: Economic Survey (FY 2015/16) and Quarterly Economic Report (FY 2015/16).

The growth trend of government's revenue and expenditure of the government of Nepal over the period of 1990/91-2015/16 is also depicted in Figure 4.6.

Figure 4.6
Growth Trend of Government's Revenue and Expenditure (at current prices)



Source: Table 4.6

Figure 4.6 shows the growth trend of expenditure, government revenue with grants and without grants which is in fluctuating with ups and down trend. The average growth rates are 99.51%, 201.17% and 52.38% of expenditure, government revenue with grants and without grants respectively.

4.2.2 Expenditure Coverage by Revenue

Table 4.7 shows the expenditure coverage by revenue with foreign grants and without foreign grants of Nepal from FY 1990/91 to FY 2015/16. Its total amount and percentage share in total expenditure is in increasing trend during the review period.

Table 4.7
Expenditure Coverage by Revenue (at current prices)

Fiscal Year	Expenditure Coverage by Revenue with Grants (%)	Expenditure Coverage by Revenue without Grants (%)
1990/91	54.75	45.56
1991/92	57.37	51.15
1992/93	61.30	49.03
1993/94	65.41	58.28
1994/95	73.00	62.92
1995/96	70.30	59.93
1996/97	71.69	59.88
1997/98	68.32	58.69
1998/99	69.80	62.52
1999/00	73.34	64.72
2000/01	69.70	61.24
2001/02	71.35	63.00
2002/03	78.60	66.94
2003/04	80.23	69.69
2004/05	81.19	68.37
2005/06	76.29	65.18
2006/07	76.71	65.65
2007/08	77.63	66.70
2008/09	75.72	65.32
2009/10	83.38	69.29
2010/11	82.71	67.65
2011/12	84.08	72.11
2012/13	94.12	82.46
2013/14	93.98	85.81
2014/15	84.74	76.35
2015/16	71.74	57.96
Average	74.90	64.48

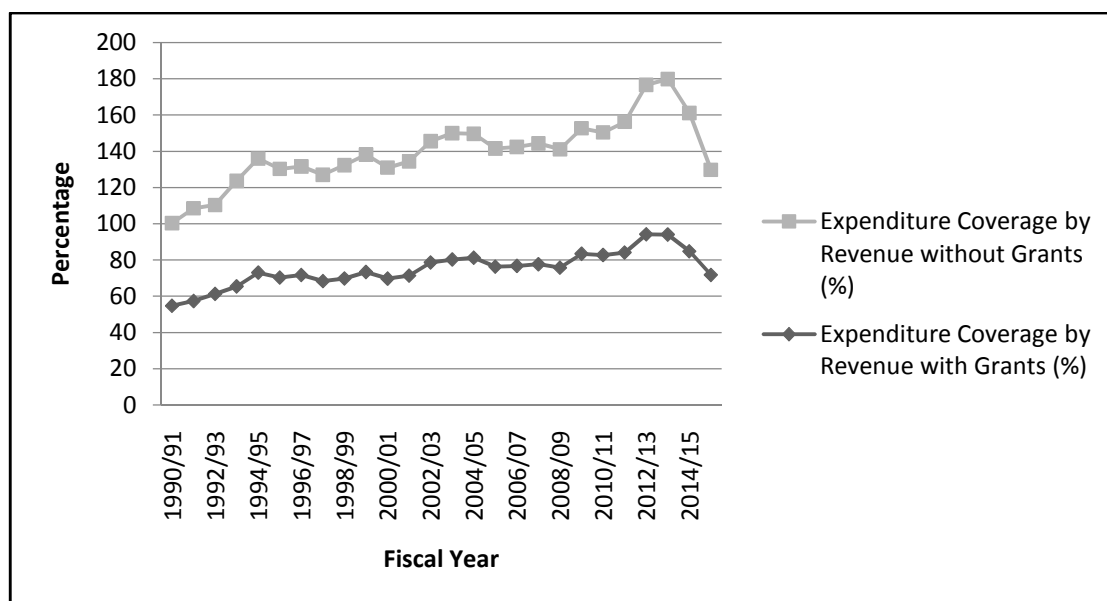
Source: Economic Survey (FY 2015/16) and Quarterly Economic Report (FY 2015/16).

Table 4.7 shows the expenditure coverage by government revenue with foreign grants and without foreign grants. The total government expenditure has greater than total government revenue with foreign grants and without foreign grants. The contribution of total government revenue with foreign grants to expenditure has covered only

54.75%, 57.37%, 61.30%, 65.41%, to FY 2001/02. Similarly the contribution of total government revenue with foreign grants to expenditure from FY 2002/03 to FY 2015/16 is 80.23%, 81.19%, 76.29%, 76.71%, 77.63%, 75.72%, 83.38%, 82.71%, 84.08%, 94.12% and 93.98%, 84.74%, and 71.74% respectively. While the government revenue with grants in the FY 2012/13 recorded a higher growth rate. The expenditure coverage by government revenue of the corresponding period of current fiscal year in comparison of the expenditure of the previous fiscal year has risen. From above table and figure shows the government revenue is less than government expenditure so that the government always depends to the internal loan and external loan.

The expenditure coverage by government revenue with grants and without grants to total of the period of 1990/91-2015/16 is also depicted in Figure 4.7.

Figure 4.7
Expenditure Coverage by Revenue (At Current Prices)



Source: Table 4.7

From Figure 4.7 the government revenue has been increasing trend so that its coverage to expenditure is also gradually increasing. The graph shows the expenditure coverage by government revenue with grants and without grants is ups and down with increasing figure over the period of FY 1990/91 to 2015/16. It shows satisfactory contribution in current fiscal year compare to previous fiscal year. However the total government revenue has not sufficient to government expenditure over the study period FY 1990/91 to 2015/16.

4.2.3 Total, Recurrent and Capital Expenditure Coverage by Tax Revenue

Table 4.8 shows the recurrent, capital and total expenditure coverage by tax revenue of Nepal from FY 1990/91 to FY 2015/16. Table 4.8 shows the expenditure of recurrent is higher than other expenditure. The tax revenue covers to recurrent expenditure is 146.24% in FY 1994/95, 84.33% in FY 2010/11 106.11% in FY 2013/14 and 88.18% in FY 2015/16. The trend of recurrent expenditure coverage is % in overall study period. The capital expenditure covers by tax revenue is 51.17% in FY 1990/91 and 511.58% in FY 2015/16. The trend of capital expenditure coverage is gradually increasing until in FY 2015/16. The average capital expenditure coverage is gradually increasing until in FY 2015/16 but not full over by tax revenue. The average coverage of total expenditure is 51.79% in overall period.

Such scenario of expenditure took place in the Nepalese budgetary history because of insurgency and political instability and then political transition in the country. The absolute amount of expenditure is increasing from initial to the final year of the study period. But the implement is fluctuating in trend. The uncontrolled increase in government expenditure accompanied by constantly low level of revenue realization has been mainly responsible for acceleration in government fiscal and deficit. Causes of deficit are quite clear from the above shows that the level of government expenditure have been higher than the level of revenue including foreign grants. The gap between revenue sources and total expenditure was widened significantly during the review period. It amply shows the fact that the government has not been able to meet the growing expenditure.

Table 4.8**Recurrent, Capital and Total Expenditure Coverage by Tax Revenue**

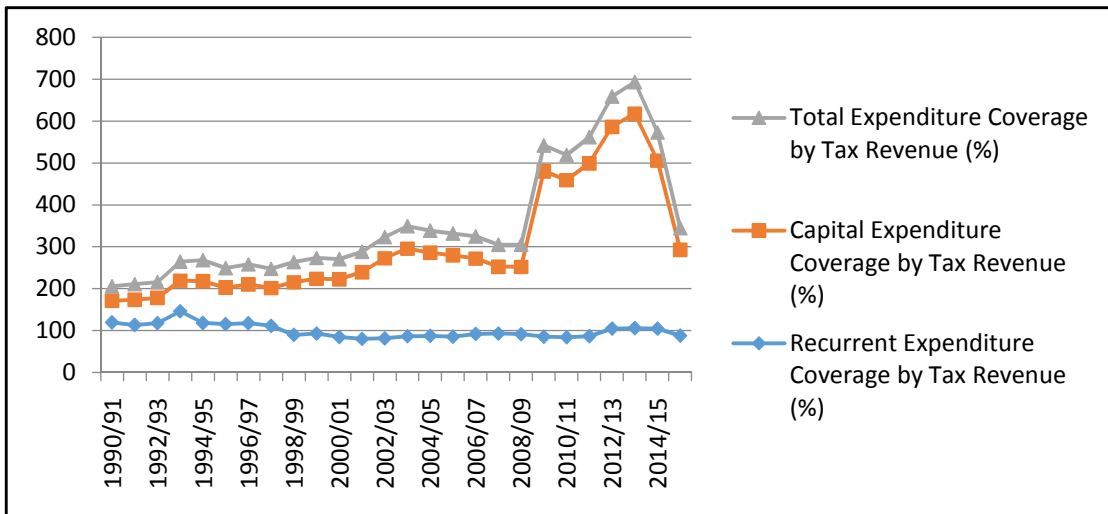
Fiscal Year	Recurrent Expenditure Coverage by Tax Revenue (%)	Capital Expenditure Coverage by Tax Revenue (%)	Total Expenditure Coverage by Tax Revenue (%)
1990/91	119.69	51.17	34.72
1991/92	113.54	59.81	37.38
1992/93	117.97	60.07	37.75
1993/94	146.24	72.55	45.75
1994/95	118.35	99.32	50.33
1995/96	115.78	86.74	46.56
1996/97	117.83	92.02	48.15
1997/98	111.54	89.58	46.20
1998/99	90.01	125.06	48.26
1999/00	93.17	130.09	50.02
2000/01	84.79	137.30	48.68
2001/02	80.49	158.77	49.12
2002/03	81.76	190.49	50.70
2003/04	86.72	208.59	53.86
2004/05	87.71	197.90	52.76
2005/06	85.69	193.97	51.79
2006/07	92.28	179.13	53.27
2007/08	93.11	159.11	52.77
2008/09	91.63	160.15	53.29
2009/10	85.63	394.44	61.53
2010/11	84.33	374.47	60.00
2011/12	86.96	411.99	62.42
2012/13	105.11	480.97	72.37
2013/14	106.01	511.58	75.18
2014/15	104.87	400.66	66.97
2015/16	88.18	204.43	52.11
Average	99.59	201.17	52.38

Source: Economic Survey (FY 2015/16) and Quarterly Economic Report (FY 2015/16).

The recurrent, capital and total expenditure coverage by tax revenue of Nepal over the period of 1990/91-2015/16 is also depicted in Figure 4.8.

Figure 4.8

Recurrent and Capital and Total Expenditure Coverage by Tax Revenue



Source: Table 4.8.

Figure 4.8 shows the trend of recurrent, capital and total expenditure coverage by tax revenue. The coverage of capital and total expenditure shows the increasing trend and the coverage of recurrent expenditure shows the decreasing trend. Tax revenue is not sufficient income for the government expenditure.

Most of the countries in the world practice the budget deficit. Theoretically the volume of expenditure surpasses the in such situation as such gap between the expenditure and revenue needs to be managed with various instruments. In other words, the budgetary and fiscal deficit ought to be financed. In the Nepalese context, as elsewhere, budgetary and fiscal deficit are financed with the medium of internal and external sources, External sources include foreign assistance, particularly loans and grants where internal sources includes internal loan along with borrowing and cash surplus. To meet overall deficit an external sources of financing such that loan grants are found in heavily used. Therefore it can be noted that external sources of financing have crucial role in the Nepalese economy.

4.3 Trend and Composition of Revenue

Total revenue of Nepal can be decomposed into tax revenue and non-tax revenue. Tax revenue contributes about three quarters of total revenue while non-tax revenue represents about the quarter of total revenue. This is shown in table 4.9 and figure 4.9. During the study period, the amount of both tax and non-tax revenue in absolute term has increased. In FY 2002/03, the amount of tax and non-tax revenue were Rs. 4258.69 ten million and Rs. 1364.29 ten million respectively. In the FY 2006/07, the

share of tax revenue and non-tax revenue on total revenue were Rs. 7113.41 ten million and 1658.53 ten million respectively. Similarly, the contribution of tax revenue and non-tax revenue for the FY 2009/10 were Rs. 15466.77 ten million and Rs. 2427.83 ten million respectively. In percentage term, the contribution of tax revenue and non-tax revenue on total revenue for the FY 2009/10 was 85.90 percent and 14.10 percent respectively. These contributions were increase to 81.09 percent and 18.91 percent respectively in the FY 2006/07. And for the FY 2015/16, their contributions were 88.78 percent and 11.22 percent respectively. The dominant role of tax revenue is thus, quite satisfactory as its amount has been increased more significantly than the non-tax revenue over the period 2002 to 2015/16.

The non-tax revenue comes to the form of fees, fines, penalties, dividend, interest, sales of goods and services and so on. There is some source for generating more revenue through the rationalization of non-tax source particularly by improving pricing policies and operational performance. These sources can not be used effectively as a revenue raiser since most of these sources are levied not for revenue purpose.

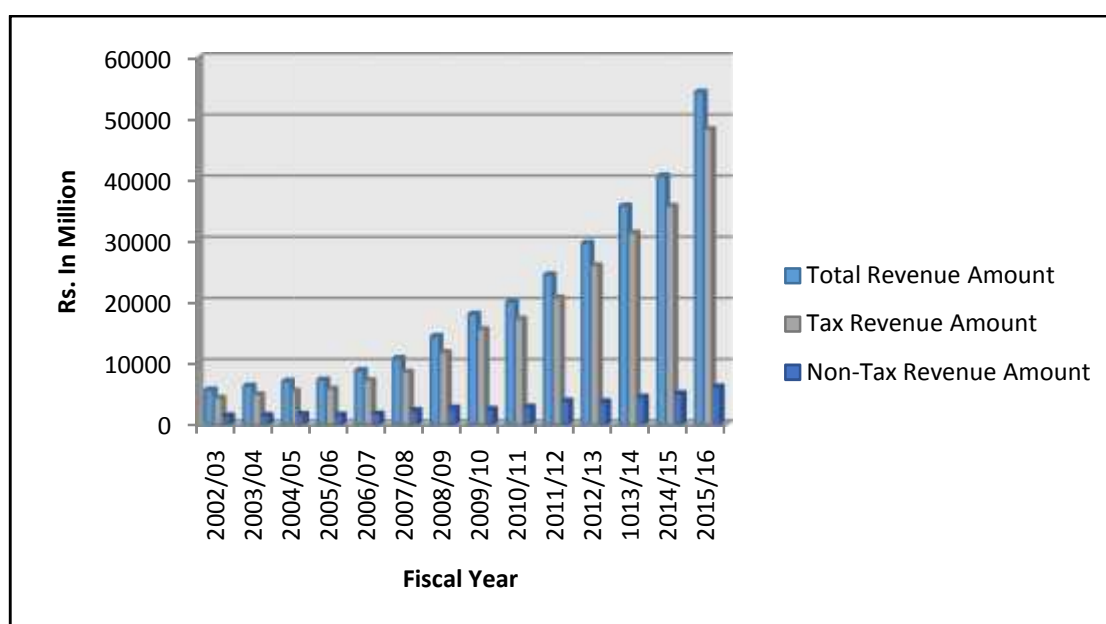
Table 4.9
Contribution of Tax and Non-tax Revenue to Total Revenue

Fiscal Year	Total Revenue		Tax Revenue		Non-Tax Revenue	
	Amount	Percent	Amount	Percent	Amount	Percent
2002/03	5622.98	100	4258.69	78.47	1364.29	21.53
2003/04	6233.1	100	4817.3	81.25	1415.8	19.75
2004/05	7012.27	100	5410.47	79.94	1601.8	21.06
2005/06	7228.2	100	5743.04	81.54	1485.16	18.46
2006/07	8771.19	100	7113.41	81.09	1658.53	18.91
2007/08	10754.6	100	8502.49	79.06	2252.12	20.94
2008/09	14347.5	100	11705.2	81.58	2642.26	18.42
2009/10	17994.6	100	15466.8	85.9	2427.83	14.1
2010/11	19981.9	100	17182.3	86	2799.59	14
2011/12	24414.9	100	20636.1	84.5	3778.79	15.5
2012/13	29593.7	100	25914.4	87.57	3679.29	12.43
2013/14	35662.1	100	31244.1	87.61	4417.95	12.39
2014/15	40584.6	100	35594.3	87.70	4990.35	12.30
2015/16	54288.4	100	48196.6	88.78	6091.78	11.22

Source: Economic Survey (FY 2015/16) and Quarterly Economic Report (FY 2015/16).

Total revenue of the government comprises tax revenue and non-tax revenue. Comparing the contribution of both sources on total revenue, always tax revenue plays vital role on it. There are three fiscal year 2002/03, 2004/05 and 2007/08 in which the contribution on non tax revenue crosses 20 %, but in other fiscal year till 2015/16, there is always less than 20 % on total revenue. This information also presented in figure 4.9.

Figure 4.9
Trend and Composition of Total Revenue



Source: Table 4.9

4.4 Tax Structure of Nepal

Excluding foreign aid, tax is the main income source of nation's budgetary generation. For self-reliance in economic growth of the economy, the government has to extend the domestic and international tax value generating the various resources and increase the per capita income of the people. For the developing countries like Nepal, the role taxation in the process of economic development is thus considerably significant. In this respect, the tax structure has vital role in economic development. Government has introduced several taxes mainly to raise revenue. The trend and composition of tax revenue in the recent years is examined here.

4.4.1 Trends and Composition of Tax Revenue

Total tax revenue is composed of direct tax and indirect tax. During the Study period, there has been simultaneous increase in total, indirect and direct tax revenue as shown in table 4.2 and figure 4.2. In FY 200/03, the amount of total, direct and indirect tax revenue were Rs. 4258.9 ten million, Rs. 1257.49 ten million and 3001.41 ten million respectively. These amounts were increased to Rs. 7113.41 ten million, Rs. 1898.77 ten million and Rs. 5214.64 ten million respectively in the FY 2006/07. In the FY 2015/16, these amounts were Rs. 42104.9 million, Rs.14949.9 ten million and Rs. 27155.4 ten million respectively.

Though the direct and indirect tax revenue in absolute term increased during the study period, its contribution in total revenue in percentage term increase from 70.48 percent in FY 2002/03 to 75.84 percent in 2004/05. But the share of indirect tax in total tax revenue decreased to 74.06 percent in FY 2009/10. Similarly, in the FY 2010/11 decreased to 72.24 percent.

Nevertheless, the indirect tax revenue still contributes about three quarters of total tax revenue while direct tax revenue represents only about one quarter of total tax revenue. It would, however not be very difficult to understand as to why the indirect tax has got the lion share in the total tax revenue. The industries have not been developed adequately. The population is dominated by the subsistence economy where per capita income is very low.

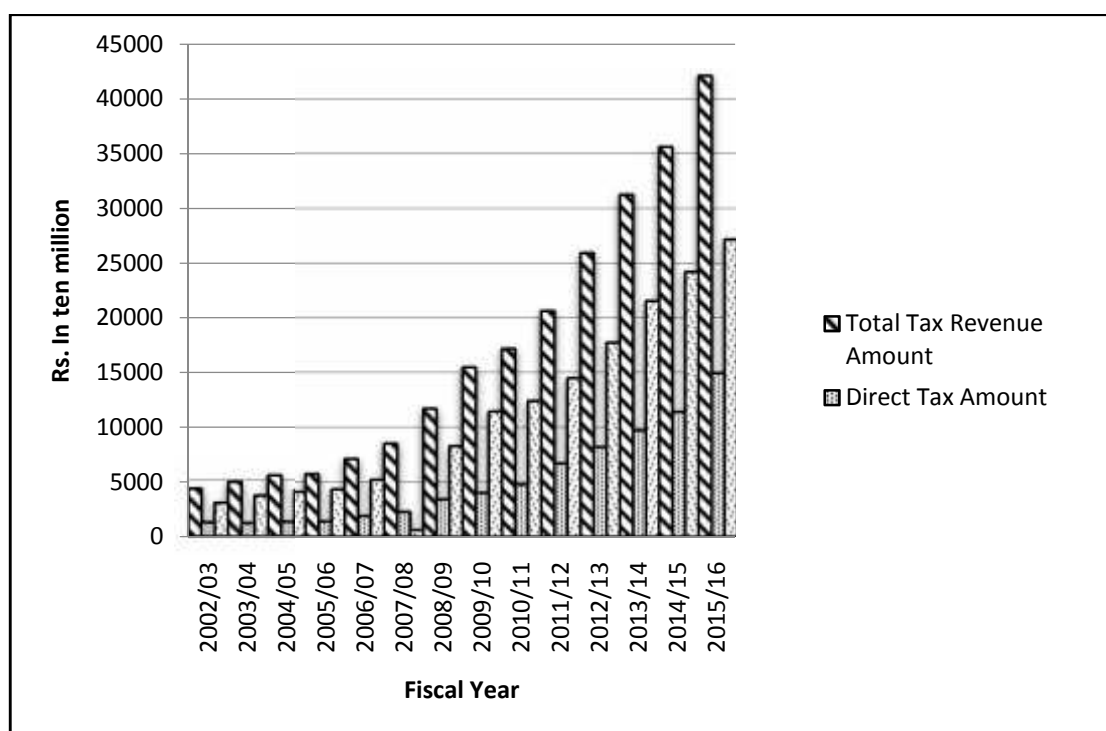
In the Nepalese perspective; while the direct tax seems to be justified, the indirect tax is unavoidable. The direct tax is justified because it helps to mobilize revenue for the national exchequer and also assists to narrow the gap in the distribution of income and wealth between the richer and the poorer sections of the society, which is essential for development. However, under the existing circumstances, the direct tax cannot generate sufficient revenue to the national exchequer. It is only through the indirect tax that adequate revenue can be mobilized and the consumption of harmful commodities or the investment in the unproductive sectors of the economy can effectively be discouraged. Thus, though there is the need for Nepal government to rely upon the direct tax, which would have a more dominating role in the Nepalese economy, at least for mobilizing adequate resources for development.

Table 4.10**Contribution of Direct and Indirect Tax Revenue on Total Tax Revenue**

Fiscal Year	Total Tax Revenue		Direct Tax		Indirect Tax	
	Amount	Percent	Amount	Percent	Amount	Percent
2002/03	4258.9	100	1257.49	29.52	3001.41	70.48
2003/04	4817.3	100	1191.26	24.72	3626.04	75.28
2004/05	5410.47	100	1307.18	24.16	4103.29	75.84
2005/06	5743.04	100	1396.81	24.32	4346.23	75.68
2006/07	7113.41	100	1898.77	26.69	5214.64	73.31
2007/08	8502.49	100	2295.72	27	626.77	73
2008/09	11705.2	100	3432.07	29.32	8273.12	70.68
2009/10	15466.8	100	4012.28	25.94	11454.5	74.06
2010/11	17182.3	100	4769.99	27.76	12412.3	72.24
2011/12	20636.1	100	6690.67	32.42	14481.2	70.17
2012/13	25914.4	100	8193.75	31.62	17720.6	68.38
2013/14	31244.1	100	9706.54	31.067	21537.6	68.93
2014/15	35594.3	100	11399.1	32.03	24195.2	67.97
2015/16	42104.9	100	14949.5	35.51	27155.4	64.49

Source: Economic Survey (FY 2015/16) and Quarterly Economic Report (FY 2015/16).

Figure 4.10
Trend and Composition of Tax Revenue



Source: Table 4.10

4.4.2 Trend and Composition of Direct Tax

In Nepal's tax structure, the main components of direct tax are income taxes are income tax and land registration taxes. In FY 2002/03, their contributions in total direct tax revenue were Rs. 1027 ten million and Rs. 61 ten million respectively as shown I table 4.11 and figure 4.11. The remaining part of the direct tax was covered by other direct taxes. During the same period, the contributions in percentage term were 81.67 percent, 4.85 percent and 13.48 percent respectively.

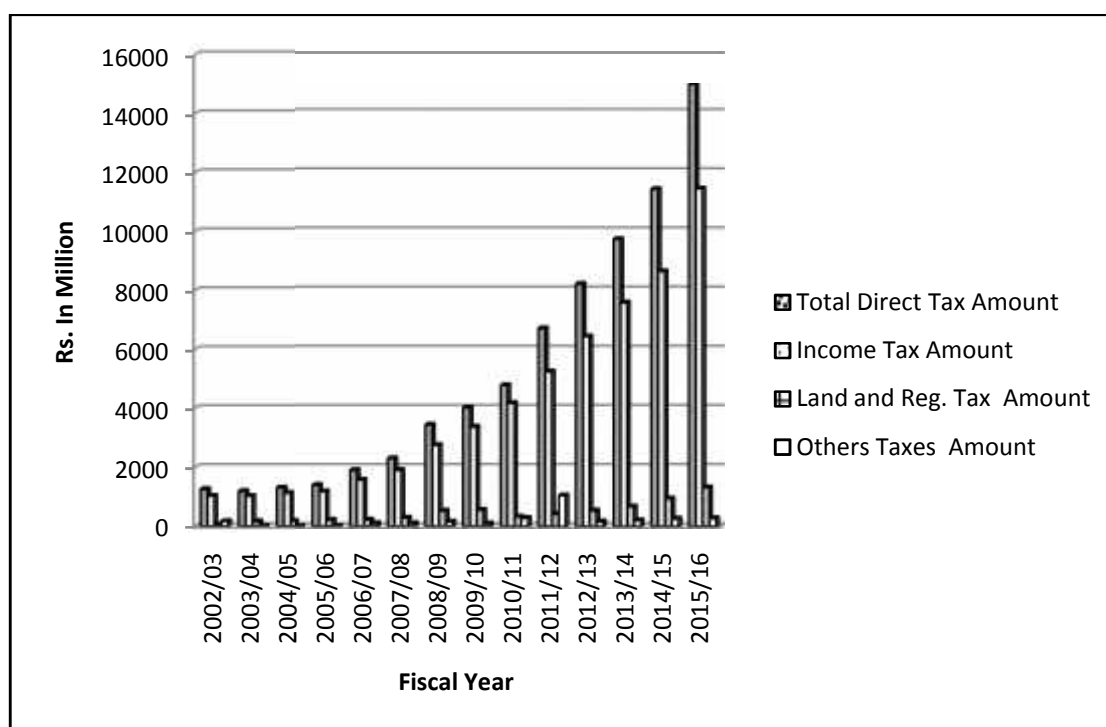
The share of income tax (85.70%) in FY 2003/04 was increased to 86.21 percent in FY 2004/05. But, this contribution was decreased to 82.48 percent in FY 2006/07 and again increased to 87.37 percent in FY 2010/11. the share of land and registration tax in direct tax in FY 2002/03 (4.85%) was also increased to 14.27 percent in FY 2003/04, and again increased to 15.60 percent in FY 2005/06. The other tax includes tax on property, profit and income. It can be concluded that direct tax is increasing trend up to 2015/16.

Table 4.11
Composition of Direct Tax Revenue

Fiscal Year	Total Direct Tax		Income Tax		Land and Reg. Tax		Others Taxes	
	Amount	Percent	Amount	Percent	Amount	Percent	Amount	Percent
2002/03	1257.49	100	1027	81.67	61	4.85	169.49	13.48
2003/04	1191.26	100	1021	85.7	170	14.27	0.26	0.03
2004/05	1307.18	100	1127	86.21	180	13.77	0.18	0.01
2005/06	1396.81	100	1179	84.4	218	15.6	0.19	0.01
2006/07	1898.77	100	1573	82.84	225	11.84	100.77	5.32
2007/08	2295.72	100	1903	82.89	292	12.71	100.72	4.4
2008/09	3432.07	100	2748	80.06	525	15.29	159.07	4.65
2009/10	4012.28	100	3365	83.86	550	13.7	97.28	2.44
2010/11	4769.99	100	4168	87.38	320	6.7	281.99	5.93
2011/12	6690.67	100	5233	78.21	414	11.8	1043.67	15.60
2012/13	8193.75	100	6417.83	78.33	530.9	6.48	160.59	1.96
2013/14	9706.54	100	7560.92	77.90	664.28	6.84	200.81	2.07
2014/15	11399.1	100	8616.8	75.59	938.63	8.23	257.19	2.26
2015/16	14949.5	100	11416.9	76.37	1314.13	8.79	271.14	1.81

Source: Economic Survey (FY 2015/16) and Quarterly Economic Report (FY 2015/16).

Figure 4.11
Composition of Direct Tax



Source: Table 4.11

4.4.3 Trend and Composition of Indirect Tax

The indirect tax in this study refers to three categories of taxes: Customs duties, VAT, and Excise duties, which contributes about 60 percent of total revenue in the study period. Their initial amount in FY 2002/03 were Rs. 1278.32 ten million, Rs. 1345.97 ten million and Rs. 377.12 ten million respectively as shown in table 4.12 and in figure 4.12.

In percentage term, the contribution of customs duties, VAT and Excise duties in total indirect tax were 42.59 percent, 44.84 percent and 12.56 percent respectively in 2002/03. The remaining portion of the indirect tax was covered by other indirect taxes. Of the total indirect tax revenue realized during the study period, customs duty constituted the highest share followed by VAT and excise duty. Despite the dominating shares of customs duty in total indirect taxes, its future is rather disappointing.

The table shows that the contribution of VAT to total indirect taxes has increased quite significant because of the imposition of VAT. In FY 2002/03, its contribution was 44.48 percent in total indirect tax. In FY 2004/05, its share increased to 46.02

percent, in 2005/06 its share increased to 49.72 percent and in 2006/07 its share further increased to 50.04 percent. Improvement in VAT implementation is the main reason for such a satisfactory performance. Thus, the revenue from VAT has been increasing more significantly than other components (Customs and excise duties) in the total indirect tax revenue. It can be concluded that VAT has higher contribution in indirect tax.

Table 4.12
Composition of Indirect Tax Revenue

Fiscal Year	Total Indirect Tax	Customs Duties		VAT		Excise Duties		Other Tax	
	(Rs in Ten Million)	(Rs in Ten Million)	Percent	(Rs in Ten Million)	Percent	(Rs in Ten Million)	Percent	(Rs in Ten Million)	Percent
2002/03	3001.41	1278.32	42.59	1345.97	44.84	377.12	12.56	44.25	1.47
2003/04	3626.04	1555.48	42.89	1447.89	39.93	622.67	17.17	47.81	1.31
2004/05	4103.29	1570.16	38.26	1888.54	46.02	644.59	15.7	51.63	1.25
2005/06	4346.23	1534.4	35.3	2161.07	49.72	650.76	14.97	65.94	1.51
2006/07	5214.64	1670.76	32.03	2609.56	50.04	934.32	17.91	47.63	0.91
2007/08	6206.77	2106.24	33.93	2981.57	48.03	1118.96	18.02	49.16	0.79
2008/09	8273.12	2679.29	32.38	3970.09	47.98	1622.09	19.96	72.88	0.88
2009/10	11454.49	3515.08	30.68	5492.09	47.94	2430.61	21.21	75.92	0.66
2010/11	12412.26	3571.16	28.77	6166.36	49.67	2654.29	21.38	104.18	0.83
2011/12	11481.16	4340.98	37.81	7066.93	61.55	3025.62	26.35	490.7	4.27
2012/13	17720.61	5691.49	32.12	8339.11	47.06	3624.4	20.45	65.61	0.37
2013/14	21537.56	6798.06	31.56	1011.06	4.69	4541.10	21.08	87.34	0.41
2014/15	24195.18	7484.45	30.93	11251.8	46.50	5354.03	22.13	104.88	0.43
2015/16	27155.39	8218.55	30.26	12231.5	45.04	6576.83	24.22	128.5	0.47

Source: Economic Survey (FY 2015/16) and Quarterly Economic Report (FY 2015/16).

4.4.4 Total Revenue, Tax and Non Tax Revenue in GDP

In order to understand the growth pattern of taxation properly, it would be desirable to examine the share of total revenue, tax revenue and non-tax revenue and non tax 4.5 in this connection presents an account of the total, tax revenue and non tax revenues as percentage of GDP. In the GDP, tax revenue has been increasing much higher than the non tax revenue over the period 2002/2003 to 2015/2016 and for the period 2009/010, tax revenue also increased much in comparison with non tax revenue.

Table 4.12**Total Revenue, Tax Revenue and Non Tax Revenue as Percentage of GDP**

Fiscal Year	GDP (Rs in Ten Million)	Total Revenue (Rs in Ten Million)	Tax Revenue	Non-Tax Revenue (Rs in Ten Million)	% of GDP		
					Total revenue/GDP ratio	Tax/GDP ratio	Non-tax/GDP ratio
2002/03	49223.10	5622.98	4258.69	1364.29	11.42	8.65	2.77
2003/04	53674.90	6233.10	4817.30	1415.80	11.61	8.97	2.63
2004/05	58941.20	7012.27	5410.47	1601.80	11.89	9.17	2.71
2005/06	65408.40	7228.20	5743.04	1601.16	12.05	8.78	2.27
2006/07	72817.80	8771.19	7113.41	1658.53	13.14	9.76	2.27
2007/08	81840.10	10754.61	8502.49	2252.12	14.47	10.38	2.75
2008/09	99131.60	14347.45	11705.19	2642.26	15.21	11.80	2.66
2009/010	118268.00	17994.60	15466.77	2427.83	14.59	13.07	2.05
2010/011	136943.00	19981.88	17182.25	2799.59	15.66	12.54	2.04
2011/012	155817.40	24414.88	20636.07	3778.79	15.67	13.24	2.42
2012/13	169264.30	29602.11	25921.49	3680.62	17.5	15.3	2.2
2013/14	194162.40	35662.07	31244.12	4417.95	18.2	15.9	2.2
2014/15	212047.00	40586.64	35595.57	4991.07	19.1	16.8	2.4
2015/16	224869.10	47501.21	42701.10	4800.11	20.5	18.4	2.1

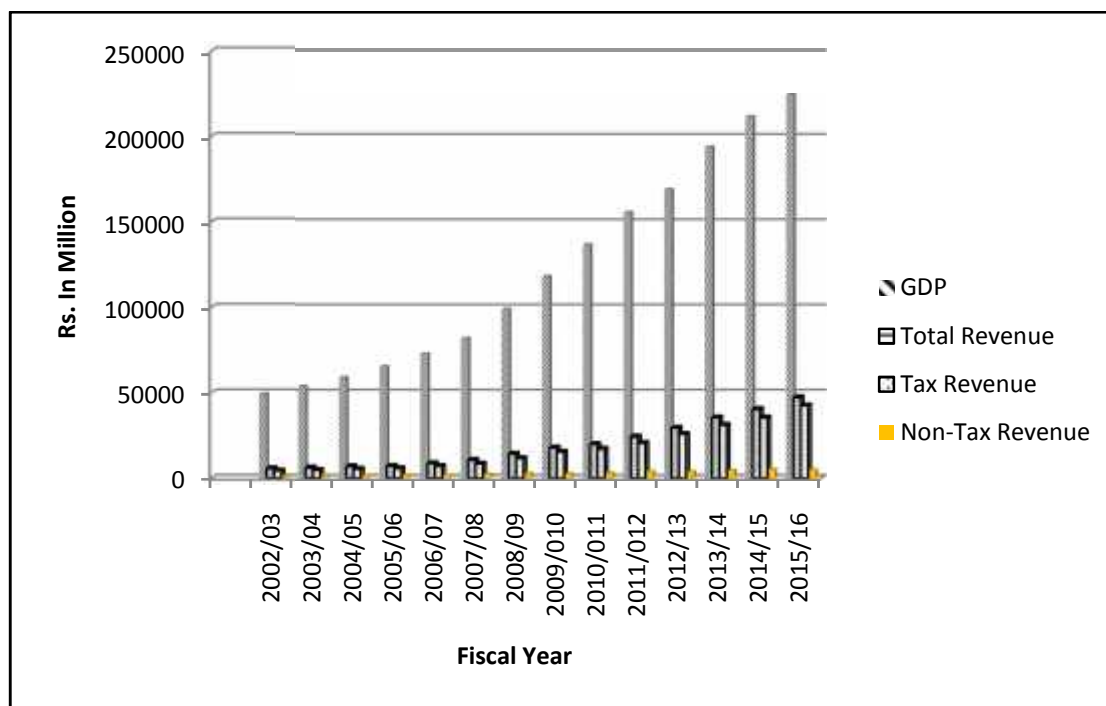
Source: Economic Survey (FY 2015/16) and Quarterly Economic Report (FY 2015/16).

While the share of tax revenue increased from 8.65 percent of the GDP in FY 2002/03 to 10.38 percent in FY 2006/07, the share of non tax revenue barely increased from 2.63 percent of the GDP in FY 2003/04 to 2.75 percent in FY 2007/08, the share of tax revenue and non-tax revenue of the GDP were 9.76 percent and 2.27 percent respectively in the FY 2007/08.

Whereas the share of tax revenue of the GDP was increased to 13.07 percent and decreased for non tax revenue by 2.05 percent respectively in the FY 2009/10. The relationship between tax and GDP is known as tax/GDP ratio. This is an indicator of the utilization of taxable capacity. Table 4.5 shows rather disappointing scenario of tax/GDP ratio for the study period. However, it increased from 8.65 percent in FY 2002/03 to 13.07 percent in FY 2009/10. But this growth is not continuous. The ratio

is still much lower than that of many other developing countries. By world standard this is very low level of taxation.

Figure 4.12
Tax and Non-Tax Revenues in GDP



Source: Table 4.12

4.4.5 Direct and Indirect Tax Revenue as Percentage of GDP

Table 4.6 indicates the share of direct and indirect tax revenue in GDP. In terms of GDP, the share of direct tax revenue increased from 2.55 percent in FY 2002/03 to 2.80 percent in FY 2007/08 where as the share of indirect tax revenue increased from 6.09 percent in FY 2002/03 to 7.58 percent FY 2007/08. And the share of direct and indirect tax revenue in GDP was 3.48 percent and 9.06 percent respectively in the FY 2010/11. However, this increment is not continuous. It is, thus, the indirect tax through which larger percentage of revenue is transferred to Nepal government.

Table 4.13
Direct and Indirect Tax Revenue as Percentage of GDP

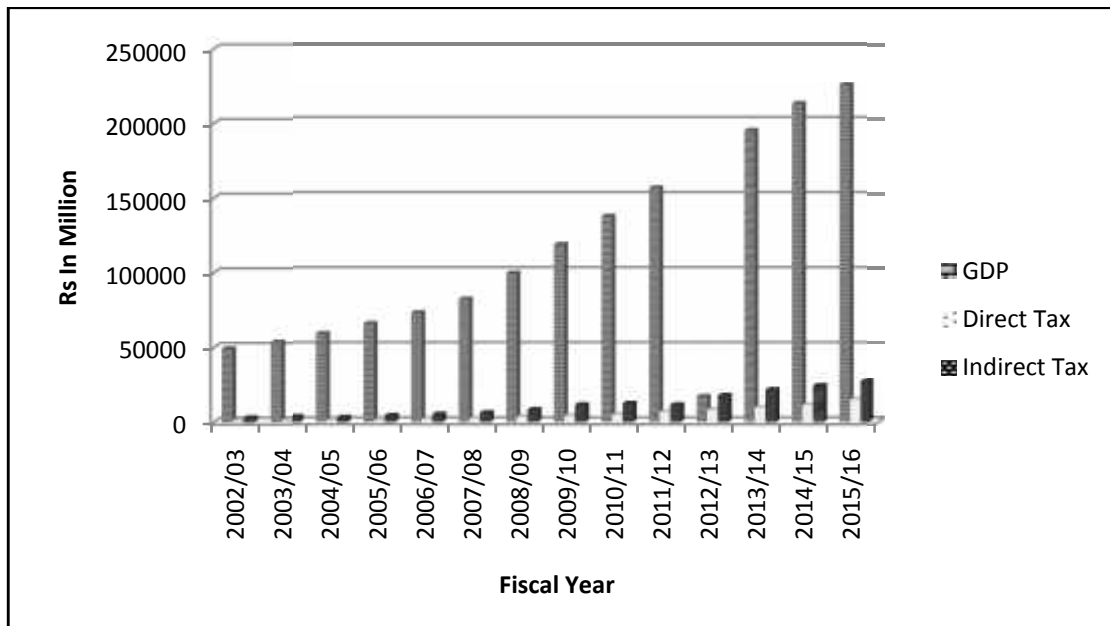
Fiscal Year	GDP(Rs in Ten Million)	Direct Tax(Rs in Ten Million)	Indirect Tax(Rs in Ten Million)	% of GDP	
				Direct Tax	Indirect tax
2002/03	49223.10	1257.49	3001.41	2.55	6.09
2003/04	53674.90	1191.26	3626.04	2.21	6.75
2004/05	58941.20	1307.18	3103.29	2.21	6.96
2005/06	65408.40	1396.81	4346.23	2.13	6.64
2006/07	72817.80	1898.77	5214.64	2.60	7.16
2007/08	81840.10	2295.72	6206.77	2.80	7.58
2008/09	99131.60	3432.07	8273.12	3.46	8.34
2009/10	118268.00	4012.28	11454.49	3.39	9.68
2010/11	136943.00	4769.99	12412.26	3.48	9.06
2011/12	155817.40	6690.67	11481.16	4.29	7.37
2012/13	16926.30	8193.75	17720.61	4.84	10.69
2013/14	194162.40	9706.54	21537.56	5.00	11.09
2014/15	212047.00	11399.1	24195.18	5.38	11.41
2015/16	224869.10	14949.5	27155.39	6.65	12.08

Source: Economic Survey (FY 2015/16) and Quarterly Economic Report (FY 2015/16).

Table 4.6 shows the direct and indirect taxes to GDP ratio. Going through the given data from the period from FY 2002/03 to 2015/16., it is observed that the contribution of indirect taxes is higher than the direct taxes. The ratio of indirect taxes remains less than 10 % in the observed period whereas the ratio of indirect taxes in term of GDP is growing in the preceding last year. This information has been depicted in the figure 4.6.

Figure 4.13

Direct and Indirect Tax Revenue as Percentage of GDP



Source: Table 4.13

Table 4.6 shows that the growth rate of GDP is rapid from FY 2008/09 onwards. Similarly, same behavior is found to the indirect taxes to GDP ratio, which is growing rapidly basically from FY 2012/13 onwards. Hence, from the given figure it is explained that in term of GDP, indirect taxes has higher contribution in compare to the direct taxes, though both are growing.

CHAPTER V

SUMMARY OF MAJOR FINDINGS, CONCLUSION AND RECOMMENDATION

5.1 Summary of Major Findings

In developing countries like Nepal, lack of sufficient financial resources is the main constraint for national economic development. A lot of fund is required to meet the additional financial requirements for the development activities of the country. Nepal has been suffering from capital shortage to accelerate the economic growth. The expenditure of Nepalese Government has been increasing year by year. To meet the additional capital requirements Nepalese government has been using external as well as internal resources.

Revenue and foreign grants are the major sources of government income. The growth rate of total tax revenue has been fluctuating with ups and down during study period. Tax revenue has registered an average annual growth of 17.28% between FY 1990/91 and 2015/2016. In comparison to FY 2012/2013, tax revenue in FY 2013/2014 decreased by 20.37%. The growth rate of tax revenue was 37.47% in FY 2008/09. The contribution of total tax revenue on total government revenue with foreign grants and foreign grants has been increased during the study period. So, it is clear that the contribution of tax revenue has been increasing but the collection of tax is not satisfactory. Government's total expenditure during the study period has been increased. The government income has covered 84.04% of total expenditure in FY 2011/12, while such coverage accounted for 94.12% in FY 2012/13. The government revenue has been covered 93.98% of expenditure in the FY 2013/14. Analyzing the sources of financing government expenditure, contribution of revenue is stood at highest.

Total revenue /GDP ratio and tax revenue/GDP ratio have been increased but non-tax revenue/ GDP ratio has been decreased during the study period. So, it is clear that the contribution of tax revenue on GDP has been increasing. Total revenue/GDP ratio and tax revenue/GDP ratio were ranged from 11.05% to 13.66% to 13.24% respectively, during the study period. The indirect tax/ GDP ratio has been increasing but direct tax revenue has been decreasing during the study period. From this, it is clear that the contribution of indirect tax on GDP has been increasing. The contribution of VAT

revenue on total revenue has been increasing during the study period. Its contribution on total revenue was average 29.7 percentages in this period. The contribution of direct tax on GDP has been increasing during study period. The direct tax/GDP ratio has ranged from 2.13% to 3.48% during the study period.

Developing countries such as Nepal utilizes external borrowing as technique to address the resource gap. The external borrowing enables the government to insure higher expenditure than would be otherwise possible. Borrowing is supposed to be the source to increase the productive capacity of the country which in some extent can contribute to alleviate poverty, minimize unemployment and stimulates for rapid economic growth.

A situation of fiscal deficit or deficit financing refers to a state wherein government' revenue including tax and foreign grant together with other receipts is less than government expenditure. As Nepal government's expenditure is higher than its income, it has been facing the situation of budget deficit or deficit financing for quite a long time. In such a situation, the governments manages funds to meet its expenditure either through the change in cash reserves or through domestic borrowing or loans foreign countries and donor agencies, or both. Due to inability of Government of Nepal to meet its expenditure from receipts of taxes, grant and principle repayment receipts, and necessary amount for expenditure is garnered by using various instrument of financing including external and domestic borrowing. It is a global practice of arranging finance by realigning foreign loan, domestic borrowing and change in cash reserve ratio in a situation when government expenditure exceeds its income level. Internal resources are preferable for sustainable economic development. Nepal has been unable for proper mobilization of internal resources. Thus, fiscal deficit and resources gap of Nepal has been increasing every year.

To solve the problems relate to tax revenue, government need to arrange the proper infrastructure and efficient revenue administration which contributes to collect revenue more. Regarding this fact, this study analyzes the important and contribution of tax revenue to the Nepalese government revenue. After identifying introduction about it, review of literature has been observed to address core elements of tax revenue and its development. Currently, tax revenue in Nepal is collected through direct tax and indirect tax. Direct tax includes income tax and land and reg. tax. Indirect tax includes customs duties, excise duties, sale/VAT tax etc. Exemption limit

and tax rate is determined according to the level and sector wise but is not adjusted according to the country and number of dependents. Exemption limit is not provided to the corporate bodies.

The success or effectiveness of tax system entirely depends upon implementation of provision, which is the major responsibility of tax revenue administration. Income tax system of Nepal has blamed as not efficient enough. Various problems existed in the income tax such as increasing habit of tax evasion, inefficient tax administration, defective tax law- are the reason of lower contribution of tax revenue.

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

In developing countries like Nepal, lack of sufficient financial resources is the main constraint for national development. A lot of fund is required to meet the additional financial requirements for the development activities of the country. Nepal has been suffering from capital shortage to accelerate the economic growth. The expenditure of Nepalese government has been increasing year by year. To meet the additional capital requirements Nepalese government has been using external as well as internal resources.

5.2 Summary of Major Findings

After analyzing the growth trends of tax and non tax revenue it is found that its position is quite weak. The growth rate of revenue is still less than 20% which indicates the poor performance of economic activities. The growth rate of tax revenue is fluctuating over the time notifies that its trend is unpredictable. Thus in this sense, it is necessary to create the predictable situation of revenue in Nepalese context, which finally helps to promote the economic growth of country.

Examining the resource coverage of tax revenue in overall resource requirement, it is found that grants covers highest chunk of pie on government expenditure. In the last fiscal year, revenue collection is just enough to finance the recurrent expenditure of the government. Development related expenditure totally depends on the other sources like loan and grant. Nepalese leadership supposes their success if they can collect more grant for the nation which have less liability. Due to this reason, still

fund for government treasure is dominated in term of capital expenditure is foreign grant and loan.

5.3 Conclusion

The role of revenue is crucial for the overall development of the country. In this context, the Nepalese government needs to develop sustainable broad based sources of revenue. Since more than 70% of the total revenue is collected from the tax sources, efficient tax system has to be developed and strengthened. In recent years, the government has taken several measures to reduce tax-induced distortions, strengthening tax administration, simplifying tax laws and procedures to make them more transparent. With an aim to Borden the tax base, the government enacted new income Tax Act in 2002. This tax act brought all sources of income from employment, business and investment-under the tax net and helped maintain neutrality of taxation in various income generating activities. The customs Act is amended to make the Nepalese system compatible with the WTO valuation system, exemptions. In 1997, the government introduced VAT aiming to develop it as the backbone of Nepalese Revenue. Unclear vision of government to the production sector, frequent changes of rules and regulations and unstable political economic environment of Nepal have sharply damage the revenue collection. However, tax laws administration in Nepal is too be deeply scrutinized and properly implemented. Act itself is not bad, some provision would have to be mentioned clearly strong commitment, fair and uniform imposition is to be stored and revitalized. Human resources development planning within the administration is desired for the efficiency of tax personal side by side, tax evasion package are to be made and imitated hence, and tax administration and tax compliance could be improved.

5.4 Policy Recommendation

The following suggestions are made in order to increase the contribution of tax on government revenue of Nepal.

- a) Tax, rules and regulation should be clear and simple for all the 'taxpayers' as well as for 'tax administration ' The definition made in Tax Act should be further clarified and well defined in simple language.
- b) The member involved in formulating tax policies must have dept knowledge about tax. The persons of rewards, price, incentives should be introduced in

the act to encourage the taxpayers to pay tax voluntarily rather through coercive measures.

- c) Separate tax department should be established so that the specialization could be achieved in matter of tax structure. Effectiveness of tax system depends upon the tax administration. In Nepal, one of the most important reasons for unsound tax system is inefficient and unscientific tax administration.
- d) Normally 15 to 18 percentage total tax revenue/ GDP ratio regarded as moderate standard. But Nepalese total revenue /GDP ratio is ranged from 11.05 percentages to 15.66 percentages only. So, government uses appropriate measures to meet the standard.
- e) The base of income tax at present is still low. The agriculture sector, which contributes around 35 percentage of national GDP, is still outside of the income tax net. It narrowed the income tax base as well as distorted the economy and had made room for tax evasion and tax planning. So the agriculture income should be taxed to broaden the income tax base. Experts should survey the modality of taxation and other measures for agriculture promotion and their recommendation should be implemented.
- f) Many potential taxpayers are still outside of the tax net such as social and education organization. Potentiality and tax evasion in this sector should be assessed and they should be brought under tax net. A separate research and analysis wing in the Inland Revenue Department should be established and it should be well equipped with skilled and professional human resource, physical and other resources is due to limitation of time and availability of data.

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