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A systematic study of income tax and revenue of Nepal in recent times

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Abstract
This present paper deals with the income tax and revenue system of Nepal. This includes historical and conceptual references to income tax and revenue system with reference to Nepal. Revenue is the backbone for the development of any country. Income tax has been put on the people by the state for the holistic development of state and people. The research focuses on the theoretical approaches adopted and implemented by the state or government.

Keywords: Income tax, revenue, state, development

Introduction

Income tax act 1799 was introduced in Great Britain firstly in the world. The aim and objective of this act was to generate revenue to afford the war with its enemy France. The Income Tax Acts were introduced in America in 1862, Italy in 1862, India in 1886, and Switzerland in 1869 and in Nepal in 1959. The notion of introducing Income Tax Act in Nepal originated from the very first 'Budget' on Magh 21, 2008 B.S. (1952). In the first budget speech, the finance minister Subarna Shamsher Rana said, "a proposal to levy an income tax, including the tax on agriculture income is under consideration." Many attempts were made to introduce income tax in the subsequent years. However, it was not submitted until 2016 B.S. (1960) due to political instability. For the first time, the Finance Act 2016 had imposed a tax on business profit and employment in Nepal (Bhattarai & Koirala 2011, 13.) In 2017 B.S. (1960), the "Business Profit and Remuneration Act 2017" was enacted which was thought the first income tax act in Nepal. This Act was found restrictive, not including many things within. There were only 22 sections containing in it. The following were the striking characteristics of this Act: Deductions were not specified for the purpose of calculating the taxable income, the cases of default fines were prescribing, a government employer was a primary income taxpayer. The experience of three years indicated that this Act was narrow. So, it was replaced by the Income Tax Act 2019 (1962.) (Bhattarai & Koirala 2011, 13.).

Objectives of the Study

The main objective of the study is to evaluate and analyze the effectiveness of income tax and revenue collection in Nepal. Some of the specific objectives of the study are as follows:

- To study and analyze the contribution of income tax from public enterprises to total tax revenue of Nepal.
- To evaluate the performance of direct and indirect tax and assess the status and prospect of direct and indirect tax in Nepal.
- To identify the problems in implementation on taxation system.
- To offer appropriate suggestions.

Conceptual framework and review of literature

Conceptual Framework

Aid interventions in revenue can support revenue mobilization for growth, improve tax system design and administrative effectiveness, and strengthen governance and compliance. The best aid modalities for revenue depend on country circumstances, but should aim to

align with government interests and facilitate effective planning and implementation of activities under an evidence based tax reform. To identifying areas for further reform requires country-specific diagnostic assessment: broad areas for developing countries identified internationally include, for example property taxation for local revenues, strengthening expenditure management, and effective taxation of extractive industries and multinationals. Government expenditure is increasing day by day because of demand of time, increase in population, social progress, increase in price, security, etc.
To meet the growing public expenditure the government has to manage its fund. It is received from different sources. To fulfillment the responsibility, the government collects revenue from public enterprises, specially assessment, fees, fines and assistance. Among them tax is main source of government revenue. In simple terminology tax is a liability to pay an amount to the government. It is compulsory contribution to the national revenue from the tax payers according to law. A compulsory from a person to the government to defray the expenses incurred in the common interest of all without reference to special benefits concerned. Taxes are general contribution of wealth of wealth levied upon persons: natural or corporate to defray expenses incurred in conferring common benefits upon the residents of the states.

The following definitions of tax clearly point out

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

Taxes are broadly divided in two categories
Direct tax
Indirect tax

Direct Tax

A tax that is paid directly by an individual or organization to the imposing entity is called Direct tax. A taxpayer pays a direct tax to a government for different purposes, including real property tax, personal property tax, income tax or taxes on assets. Direct taxes are different from indirect taxes, where the tax is levied on one entity, such as a seller, and paid by another, such a sales tax paid by the buyer in a retail setting

Indirect Tax

A tax that increases the price of a good so that consumers are actually paying the tax by paying more for the products is known as indirect tax. An indirect tax is most often thought of as a tax that is shifted from one taxpayer to another, by way of an increase in the price of the good. Fuel, liquor and cigarette taxes are all considered examples of indirect taxes, as many argue that the tax is actually paid by the end consumer, by way of a higher retail price.

Concept of Income Tax

A tax that governments impose on financial income generated by all entities within their jurisdiction by law, businesses and individuals must file an income tax return every year to determine whether they owe any taxes or are eligible for a tax refund. Income tax is a key source of funds that the government uses to fund its activities and serve the public.
Most countries employ a progressive income tax system in which higher income earners pay a higher tax rate compared to their lower earning counterparts. The first income tax imposed in America was during the War of 1812. Its original purpose was to fund the repayment of a $100 million debt that was incurred through war-related expenses. After the war, the tax was repealed, but income tax became permanent during the early 20th century.
Income tax is imposed on net income of individual and corporation must bear the burden of tax imposed on them. Generally, income means the inflow to person. Income tax is levied on the income derived from business, employment and investment. Income tax is levied on the net income i.e. total income less the allowable deduction. It is a best measure economic of a person as well as a nation.
Higher income denotes the high living standard and lower income refers to the low living standard of people. Economists define the term income in a broad sense it is an economic gain receipt to a person during a particular period by way of wages, interest, profits and rent.

The money income of the people is used for two purposes. Part of income is spent on consumption and part is saved. This definition can be understood in the given formula as below:

$Y=C+S$

Where,
Y=Income
C=Consumption

According to income tax Act 1974 (2031) "Income means the income earned or received in cash or kind from the sources as besides employment and investment." In Income Tax Act 1974 (2031) there were five heads of income tax. They were.
The new Tax Act 2058 was passed and implemented for 1st April 2002. This act defined the term as income of any person derived from employment business and investment and accumulated income calculated according to this act. This act, has classified the income into three different heads, they are:

- Business / profession
- Employment
- Investment.

Income tax refers to the tax levied on the income of a person and profits of the corporation for the specified time period, particularly one year. In a broad sense, income tax s a levy based upon the production or receipts or gain of the tax payers within a definite period of time.

Concept of Corporate Tax

Corporate tax or company tax refers to a tax imposed on entities that are taxed at the entity level in a particular jurisdiction. Such taxes may include income or other taxes.

The tax systems of most countries impose an income tax at the entity level on certain type(s) of entities (company or corporation). Many systems additionally tax owners or members of those entities on dividends or other distributions by the entity to the members. The tax generally is imposed on net taxable income. Net taxable income for corporate tax is generally financial statement income with modifications, and may be defined in great detail within the system. The rate of tax varies by jurisdiction. The tax may have an alternative base, such as assets, payroll, or income computed in an alternative manner.

Most income tax systems provide those certain types of corporate events are not taxable transactions. These generally include events related to formation or reorganization of the corporation. In addition, most systems provide specific rules for taxation of the entity and/or its members upon winding up or dissolution of the entity.

In systems where financing costs are allowed as reductions of the tax base (tax deductions), rules may apply that differentiate between classes of member provided financing. In such systems, items characterized as interest may be deductible, subject to interest limitations, while items characterized as dividends are not. Some systems limit deductions based on simple formulas, such as a debt to-equity ratio, while other systems have more complex rules.

Some systems provide a mechanism whereby groups of related corporations may obtain benefit from losses, credits, or other items of all members within the group. Mechanisms include combined or consolidated returns as well as group relief (direct benefit from items of another member).

Most systems also tax company shareholders on distribution of earnings as dividends. A few systems provide for partial integration of entity and member taxation. This is often accomplished by “imputation systems” or franking credits. In the past, mechanisms have existed for advance payment of member tax by corporations, with such payment offsetting entity level tax.

Corporations, like other entities, may be subject to withholding tax obligations upon making certain varieties of payments to others. These obligations are generally not the tax of the corporation, but the system may impose penalties on the corporation or its officers or employees for failing to withhold and pay over such taxes. A company has been defined as a juristic person having an independent and separate existence from its shareholders. Income of the company is computed and assessed separately in the hands of the company. In certain cases, distributions from the company to its shareholders as dividends are taxed as income to the shareholders.

Development of Corporate Tax in Nepal

Nepal has started informal taxation already from the beginning of the Lichhavi period. Although it has a long history of taxation, the history of corporate tax is not so far long, corporate tax was first introduced only in 1960. During the early days, corporate tax was not differentiated form the personal income tax. The same personal tax rate was imposed to the entire tax payer in progressive manner and exemption given to companies was withdrawn. Nepal originally combined corporate income tax and individual income tax, the same rate structure was designed for the corporate income and other incomes for many years. In 1986/87 a flat rate of corporate income was introduced for the Government Corporation and public Limited Corporation listing with the security exchange centre. Corporate tax was extended to private limited companies in 2050/51 and the partnership firms in 2052/53.

Income Tax Act 1974 was introduced with new provisions. The finance act under this act introduced a separate provision for the companies. Similarly, the finance act 1985 made provisions of giving 5 percent tax rebate from higher marginal rate of 55 percent to listed public companies and the government enterprises. The FY 1986/87 changes the nature of tax rate to the corporate bodies (companies) from the progressive tax rate to flat tax rate. In this time the tax rate was 40 percent flat rate for all listed companies. The same finance act imposed tax on the divided also to be deducted at the source rate of 20 percent. But the divided tax system was changed exempting dividend to a level of 85 percent in 1987/88 and the scent percent in 1990/91. Compulsory self-tact assessment system for public and private limited companies was introduced in the Finance act 2049. The additional change was made that be taxing corporate income at flat rate to the private limited company and enacted from the financial year 2051/52. This change abolished the discrimination between private companies and public companies. Another major change carried out by FY 2055/56 was the inclusion of dividend of the non- industrial companies within the tax net. The initial corporate income tax amount in 1960/61 was Rs. 255 Millions. It was increased to 60percent in the FY 1975/76. It was dropped to 50 percent in 1979/80 and continues to 1981/82. Once again, the rate was increased up to 55 percent in 1982/83 and was stable for 3 years i.e. up to 1986. And declined thereafter to 40 percent and 30 percent for up to 1991/92 and now this rate is 20 percent for special industry and 25 percent for the general industry and 30 percent for the bank and finance companies.

Corporate Income Tax

Corporate Income tax is a compulsory levy of the government. It is levied on corporate income. Since the fiscal year 1986/87, the corporate income tax has been introduced. Initially the government enterprises and listed companies in security exchange center of Nepal were paying corporate income tax on their net profit assessed by the tax officer (Finance Act, 1986).

The income from PEs, Semi PES, Public Ltd. Companies and Private ltd. companies are actually treated as the corporate income for the corporate income tax in position. Private Ltd. Companies are established and managed by one or more owner but the public limited companies are established in participation of a large number of shareholders and managed by a team of experts of different discipline. These both companies are run to maximization of profit or wealth but PEs are established to maximize public interest rather than profit maximization and they are owned by government (Pradhan, 2058: 42).

The after tax profit is disposable income of the taxpayers. High rate of corporate income tax minimizes disposable income and vice versa. The big stockholders of the corporation are in position to control and they are aware, with the corporate income tax. PEs is run by the government and the whole amount of income generated by those enterprises is belonged to the government either in form of corporate income tax or in form of reserve and surplus or dividend. The government can withdraw the amount from PEs but cannot take out from the public limited, companies and private limited companies. Though private and public limited companies are crucial in corporate income tax, PEs also contributes in this Meld keeping its public interest objective (Bhattarai, 2054:15). PES holds the second top most place of whole income tax structure.

In developing country like Nepal, the corporate development is very necessary for the economic development process. Therefore, it is required to exploit the available resources of the country. The corporate body would generate income through the exploitation of resources of the country and the government levies taxes. When corporate development takes place in a country and corporation are able to generate more revenue, automatically the government can collect a substantial amount of revenue through corporate income tax.

Corporate Tax Planning

Tax planning is also one of the ways of reducing the tax amount by the taxpayer. However, in contrast to tax evasion, tax avoidance and tax delinquency, it is legal, ethical and economic.

The word “tax planning” is made from the combination of two words taxes planning. Tax means compulsory payment to the government and claiming means taking decision about the futures by choosing the best from different alternatives. Every business organization has to make decision while conducting as business activities. That means every; business organization uses to plan as regards its future activities. Such, future activities may be of short term, medium term or long term and operational or strategic. If tax factor is considered while planning the business activities of an organization, it is tax planning. For the purpose of enhancing the investment environment in a country, the government provides different types of facilities to the business organizations. Such facilities include reduction in tax rate, providing tax holiday. Investment allowances, depreciation facility etc. tax planning means the use of all these facilities given by the government to reduce the tax liability. In other words, tax planning is the scientific planning of the companies' operations in such a way as to attract minimum liabilities of tax or the postponement of tax liability for the subsequent period by availing of various incentives, concessions, allowances, rebates and relieves. It is not only the planning of infrastructure of the business and industries but also the planning of its various projects from time to time and its day to day activities so as to acquire the maximum facility as per the existing law of the country. In short, it is a judicious use of tax incentive provided by the government. To conclude, we can say that tax planning is a scientific planning of company operations. It is economic, legal and ethical activity. It is the use of various incentives, concessions, allowances, rebates, etc. and it is an activity related to futures. It has been the following objectives:

- Reduction of tax liabilities
- Minimization of litigation,
- Productive investment,
- Healthy growth of the economy, and economic stability

(Kandel, 2060: 151)

Public Enterprises Meaning of Public Enterprises (PEs)

As stated earlier, the business units owned, managed and controlled by the state or government are termed as public sector enterprises or public enterprises. These are also known as public sector undertakings. A public sector enterprise may be defined as any commercial or industrial undertaking owned and managed by the government with a view to maximize social welfare and uphold the public interest. Public enterprises consist of nationalized private sector enterprises, such as, banks, Beema Sansthan and the enterprises set up by the government such as Nepal oil corporation (NOC), Nepal Telecom etc.

The public enterprises are owned and managed by the central or state government, or by the local authority. The government may either wholly own the public enterprises or the ownership may partly be with the government and partly with the private industrialists and the public. Autonomous or semi-autonomous organization: Public enterprise is an autonomous or semi-autonomous organization because some enterprises work under the direct control of the government and some organizations are established under statutes and companies act. The ownership with the government should be 51 percent or more to take an entity PE. Public enterprise plays a very important role in most of the developing countries. The role of public enterprises differs from country to country basically due to political philosophy of existing governments. Public enterprises come into existence either by the way of deliberate policy of the government to bring certain activities under government control by creating new institution or by nationalizing them from private sector.

In fact, public enterprises are institutions operating a service of an economic or social character, on behalf of the government, but as an independent legal entity, largely autonomous in its management, through responsible to the public, through government and parliament and subject to some direction, by the government, equipped on the other hand with independent and separate funds of its own and the legal and commercial attributer of a commercial enterprises. Public enterprises are generally owned and controlled by government and are usually autonomously organized with the government providing the initial capital and being responsible for a continuous overview of their activities. By the above definitions, one can conclude public enterprises as following features:

- Government ownership must be 51 percent or more
- Financing by the government.
- Control, direction and management by the government

Strengths of income tax for nation

1. Income tax does funding of public infrastructure in the country.
2. It does do development and welfare projects.
3. It is defense expenditure for country.
4. Income tax brings to scientific researches for country.
5. It is a public insurance for all people.
6. Income tax can be taken as an operation of the government for the state or people.

Weaknesses of income tax

1. Income tax is too complicated.
2. It is too expensive.
3. It is unfair.
4. It hides the cost of government.
5. 5 The nature of income tax is intrusive.

Suggestions

There must be transparency and simplicity in collecting and using the income tax from the people.
Collecting income tax area must be inclusive and wide for the holistic development of the nation.
There is an urgent need of proper utilization of income tax by the state or the government for the social welfare.
There must be spread awareness among all the people about the importance of paying tax on time as well as its utility.

Conclusion

Nepal falls in the category of the least developed countries in the world with low per capita income. The economic growth rate of Nepal is low, and 23. % of the total population is living below the poverty line. The financial resource gaps can be found in the context of Nepalese economy which one can say it is a major constraint of its economy. Due to the increasing gap between the expenditure incurred and revenue collection, Nepal has heavily relied on both external and internal debts to meet the budget deficit. Therefore, its economy can be tagged as a dependent economy. Among internal sources of economy of nation are of “taxation”. Taxation is a prime determining factor for the development of the nation. It is called the pillar of the fiscal policy for nation. The present study based on secondary researches, entitled, “A Sytematic Study of Income Tax and Revenue of Nepal” highlights the importance of tax for the development of the nation.

In this study, the vital role of income tax for the welfare of the people is critically examined. Numerous books, articles and other suitable material were covered and analyzed during the study for finding the useful findings on the role of income tax for nation. Various concepts of collecting taxation are discussed here in order to find the useful insights. Sources of the government revenue, the meaning of tax, tax classification, historical background of income tax, heads of income, etc. have been taken into consideration. The government of Nepal requires ample sources of revenue to launch and run the development programs, handle day to-day operations, keep peace and security, and launch other public welfare activities. The government revenue should be augmented to fulfill the financial resource gaps in the country. Income tax is one of the dynamic tools to fulfill the economical gaps of the nation. The government collects revenue from various sources in various forms such as taxes, fees, fines, penalties, etc. Among them, taxation is the primary source of running public payments because it focuses on the most important part of government revenues. There is a dominant share of tax revenue in the Nepalese total government revenue. The contribution of tax revenue reveals a fluctuating trend as it has contributed 87.56 percent in the year 2072/73 on the total revenue but augmented to 89.87 percent in the year 2077/78. The contribution of income tax to government revenue has been fluctuating, which justifies the need to focus on appropriate implementation of income tax acts for a better revenue generation. Tax exemption limit in Nepal has continuously increased to N.R. 4,00,000 for an individual, NRS. 4,50,000 for couples and families during the year 2077/78. Corporate income tax, investment income tax and individual income tax are the major income tax types in Nepal. Corporate income tax collected from government corporations, Public Limited Companies, partnership firms, and private limited companies. An individual tax collected from remuneration, industry, business profession, etc. collected from dividend tax, interest tax, royalty, and rent tax. The share of income tax is as a percentage of GDP increased from 10.51 percent in the year 2072/73 to 19.95 percent at the end of the study period, 2077/78. This shows the share of income tax as a percentage of GDP is increasing.
The main focus of this research work is to find the contribution of income tax to national revenue of Nepal and this study also discloses that the tax revenue has the highest percentage of contribution towards the total government income of Nepal. In the Nepalese government, the income structure, tax revenue has always been greater than seven times of non-tax revenue. Among direct tax revenues, income tax revenue has played the largest role to build the nation. In recent times, the contribution of income tax in Nepal has been in an ascending order which can be a symbol of prosperity of nation if it will be utilized in a right way.

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