

CONTRIBUTION AND EFFECTIVENESS OF REMUNERATION TAX IN NEPAL

Deepak Basnet

Lecturer, Shankar Dev Campus, TU

Corresponding Author: Deepak Basnet, **Email:** deepak1984basnet@gmail.com

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Abstract

The research has been carried out with the aim to examine the contribution and effectiveness of remuneration tax in Nepal. Both primary and secondary sources of data have been used in the study. Opinion survey technique has been adopted while collecting primary data. Tax experts and employees from Kathmandu valley covering sample size 120 are taken. The remuneration tax has a significant contribution on total government revenues. Remuneration tax has 2% to 20% contribution on total income tax during ten fiscal years. Highest 22% opined unfair and weak administration is found as major problem of remuneration tax. The main factor that should be initiated to increase the contribution of remuneration tax in Nepal is making tax deduction at source (TDS) effective. The other factors should be initiated to increase the contribution of remuneration tax in Nepal are, reform in the income tax policy, rules and regulation, reduction in exemption limit and increase in tax rates.

Key words: *Professional income, defective Tax rate, unfair & weak administration, tax deduction at source (TDS), exemption limit.*

Introduction

Income tax is one of the important sources of revenue to the government. Income tax is levied by the government on the income of individuals and entities. It is one of the better sources of public revenue. To regulate the income tax in the country, income tax Act, 2058 has been enacted in 2058 B.S. After a year, the income Tax Rules, 2059 has also been enacted for the effective implementation of the objectives of the Act. This Act has classified the heads of incomes into four categories viz. employment, business, investment and windfall gain. Now, individual income tax is levied with five rates 1% for social security, 10%, 20%, 30% and 36% while corporate income tax is levied with a single or flat rate of 25%. However, banks, and financial institutes are liable to pay income tax @ 30% of taxable income (Kandel, 2011).

The remuneration taxation in Nepal was introduced in the fiscal year 1960, when the Business Profits and Remuneration tax Act, 1961 was enacted. The prevailing Nepal

Income Tax Act, 2002 has also incorporated the provision regarding tax on employment (i.e. remuneration) income. Remuneration income is the income earned by a person in a income year from the employment or service (Adhikari, 2005). Remuneration means amount given for providing services. The person getting service is called employer and the person providing service is employee. According to section 8 of the ITA 2058, an individual's income from an employment for an income year is the individual's remuneration from the employment for the year. Section 2 (aj) of the same act has given a definition that employment includes a past, present or prospective employment. It can be said that remuneration income means the income from employment or service rendered by the person to the employer in any income year (Dahal, 2004).

Income Tax Act, 2058 has included the following incomes under the head of Remuneration (employment) purpose: Salary, Wages, Allowance for specific works, Other allowances, Reimbursement of personal expenses, fees, Commission, Overtime payments, Awards, Prizes, Gifts, Bonus or incentives, Amount Received In Compensation, Payment for termination of employment, Employer's contribution to the retirement Fund and Retirement payments, Retirement Payment from government, Any other payment by the employer, Interest less than Market rate, Payments made by an employer for medical allowance. The main objective of the study is to analyze the contribution and effectiveness of remuneration tax in the income tax in Nepal.

Literature Review

'Income Tax Act, 2031' had 66 section and classified the sources or heads of income into 5 heading (categories) namely (1) Agriculture, (2) Industry, business profession or vocation, (3) Remuneration, (4) House and land rent and (5) Other sources. The act had identified the chargeable incomes and admissible expenses of each head of income. The other features of this act are provision of registration, provision of carry forward of loss, provision of common expenses, provision of self assessment of tax, provision of small taxpayer's tax assessment, provision of fine, penalty and appeal, provision of tax deduction at source, provision of tax refund, provision of tax exemptions by different other acts and rules, provision of avoidance of double taxation etc. The government also issued 'Income Tax Rules 2039' for effectively implement objectives of the Income Tax.

Remuneration is the total compensation received by an employee. It includes not only base salary but any bonuses, commission payments, overtime pay, or other financial benefits that an employee receives from an employer.

The essential features of remuneration from employment may make clear idea in order to understand the meaning of remuneration. Relationship of employer and employee, mode of payment, remuneration income and professional income, income received from employer, income received from associate of employer, income received from third party, the amount paid should be of regular nature are the essential features of remuneration tax (Amatya, 2012).

OECD (2021) carried out a research on taxation during COVID-19 and its effect. The COVID-19 pandemic has caused a significant deterioration in public finances, adding to pre-existing strains from long-term structural challenges including population ageing, climate change, rising inequality, digitalisation and automation. This report, originally prepared for G20 Finance Ministers and Central Bank Governors at the request of the Italian G20 Presidency, considers the challenges and opportunities of developing public fiscal policy strategies as countries seek to “build back better”. The report focuses in particular on how tax policy can be designed comprehensively so that fiscal systems can deliver a balance of equity, growth and sustainability, highlighting some of the key considerations that policymakers should take into account to ensure optimal tax policy design and the successful implementation of tax reform.

Kafle (2019) analyzed the causes of heavy reliance on direct tax and to analyze the volume of indirect tax revenue and direct tax revenue in total tax structure. The study found out that inefficiency in the income tax administration is due to cause of government inefficiency. The income tax to GDP, total revenue and direct tax revenue was in increasing trend. To bring program oriented fiscal policy and recommended that VAT be a major source of indirect tax in liberalized economy. For small taxpayers he suggests for door-to-door services. The study found that lack of clear, transparent and progressive economic policy is the main reason for unsatisfactory with sound effectiveness of income tax system of Nepal. Existing corporate tax rate has been found unsuitable and single rate for all types of corporation is preferred.

Amatya (2012) mentioned about Nepalese income Tax law, income year and assessment year, sources of income, concept and sources of income, concept of employment, computation of income from employment non chargeable incomes under employment common reductions income tax exemption assessment of income tax liability on employment income, surcharge and contribution of employment income to Tax revenue of Nepal. Writer has also shown about estimation and collection of employment income tax during the past decade. In this study he has clearly pointed that actual collection of employment tax is satisfactory.

There is gap between this research and the previous researches. The researchers have suggested improving the tax administration increasing the contribution of income tax in resource mobilization and winding the tax coverage. But they had not studied the remuneration tax. It also gives appropriate suggestion for correcting and improving these problems and weakness based on the primary data collected through an opinion survey with the selected people from the related area such as employees and tax experts.

Methodology

So suitable research methodology as demanded by the study has been followed. This study has mainly two aspects. They are descriptive and analytical. This chapter explains about the research design, sources of data, data collection procedure, methods of analysis of

data and tools for analysis of data. Both primary and secondary sources of data have been used in the study. Opinion survey technique has been adopted while collecting primary data. Questionnaires were distributed to income tax experts and employees so as to know their opinion towards various aspects of employment income. Tax experts and employees from Kathmandu valley covering sample size 120 are taken.

Results and Discussion

To meet the desired objective, this data presentation and analysis chapter deals with the presentation and analysis of data collected from the primary as well as secondary sources. Primary data collection has been conducted by the means of scheduled questionnaires and economic survey has been the main sources of secondary data. The response found from the respondents has been tabulated first and analysed according to objectives.

Table 1: Composition of Income Tax

(Rs. In Million)

Fiscal Year	Total Income Tax (TIT)	Corporate Tax (CT)	CT as % of TIT	Personal Income Tax (PIT)	PIT % as of TIT	House Land Rent & Interest Tax	HLRI as % of TIT	Income Tax from Remunerations (PIT)	ITRs of TIT
2007/08	25407.7	7186.5	55.7	6381.2	40.3	2940.7	5.9	2451.0	10.5
2008/09	25142.4	9425.1	50.8	9877.5	46.3	5223.3	4.9	3195.6	6.2
2009/10	31285.6	12234.4	33.6	11039.9	35.5	5511.1	4.9	4413.1	14.7
2010/11	56428.0	13965.5	24.2	13627.4	34.4	3572.5	8.4	5863.3	16.3
2011/12	51303.0	8515.8	35.1	12292.8	38.4	3588.4	7.2	1555.0	17.2
2012/13	64186.7	11578.0	33.7	15541.5	37.5	5340.2	6.7	1880.6	17.8
2013/14	75613.6	10756.6	30.5	19434.0	44.4	6671.1	6.6	2449.9	20.8
2014/15	86165.6	11574.1	40.3	22557.8	38.1	9399.4	6.3	2925.8	19.1
2015/16	105648.8	14784.7	36.7	26899.1	49.0	12044.1	5.4	3425.8	21.9
2016/17	148983.0	17343.1	11.64	34854.5	23.39	18294.0	12.28	4136.9	2.78
2017/18	159887.8	25786.3	16.13	41406.9	25.90	19332.3	12.09	5097.8	3.19
2018/19	194310.1	103252.1	53.1	62881.4	32.4	22170.4	11.4	6006.2	3.1
2019/20	219741.2	99132.4	45.1	89460.2	40.7	24640.5	11.2	6508.1	3.0
Average	95700.3	26579.6	35.9	28173.4	37.4	10671.4	7.9	3839.2	12.0

Source: *Budget Speech & Economic Survey of various years*

The range of contribution of personal income tax to total income tax is 23.39 percent to 49 percent which an average 37.4 percent during thirteen years period. Similarly, the average house, land and rent tax on total income tax revenue is 7.9 percent during study period. Likewise, about 12 percent average contribution of remuneration tax to total income tax revenue. The contribution of income tax revenue is ranged from 2.78 percent to 20.8 percent. The figure shows there is highly fluctuation in income tax collection but the tax collection is in increasing way. From the presented table we can conclude that the share of house and land rent and interest tax and remunerations tax to total tax revenue is very limited.

Contribution of Remuneration Tax

Remuneration is the total compensation received by an employee. It includes not only base salary but any bonuses, commission payments, overtime pay or other financial benefits that an employee receives from an employer.

Table 2 : Contribution of Remuneration Tax

Fiscal Year	Remuneration tax on:			
	Total government revenue (%)	Total tax revenue (%)	Direct tax revenue (%)	Income tax revenue (%)
2007/08	2.28	2.88	7.44	9.65
2008/09	2.23	2.73	9.31	12.71
2009/10	2.45	2.85	11.00	14.11
2010/11	2.93	3.41	12.29	10.39
2011/12	0.64	0.73	2.75	3.03
2012/13	0.64	0.73	2.63	2.93
2013/14	0.69	0.78	2.89	3.24
2014/15	0.72	0.82	2.97	3.40
2015/16	0.71	0.81	2.83	3.24
2016/17	0.68	0.75	2.40	2.78
2017/18	0.70	0.77	2.76	3.19
2018/19	0.82	0.93	3.05	3.09
2019/20	0.92	1.06	2.96	2.96
Average	1.26	1.48	5.02	5.75

Source: *Calculation through Excel Sheet.*

Table 2 reveals that the contribution of remuneration tax on total government revenue, total tax revenue, direct tax revenue and income tax revenue. The average contribution of remuneration tax to government revenue is 1.26 percent which is ranged between

0.64 percent to 2.28 percent during thirteen years period. Similarly, contribution to total tax revenue is 1.48 percent which is ranged from 0.73 percent to 2.88 percent. Remuneration tax has contribution to direct tax is average 5.02 percent and contribution to income tax has average 5.75 percent. The contribution of remuneration tax is found highly fluctuation during the fiscal years. The overall figure shows that remuneration tax is significant contribution to different government and tax revenues.

Empirical Investigation

An empirical investigation has been conducted from the experience of the real world in order to find out various aspects of employment income. The major tool used for this purpose is an opinion questionnaire, which was dispatched to 120 persons and responses were collected from 60 persons only. Among them, 60 were tax experts and 60 were employees.

a. Contribution of Remuneration Tax to Income Tax Revenue of Nepal

In order to know whether remuneration tax is contributing the income tax revenue or not, a question was asked, "In your opinion, is remuneration tax contributing significantly to the income tax revenue of Nepal?" The question was intended to know the respondents' opinions towards the contribution of remuneration tax in the income tax revenue. The responses received from respondents are tabulated 3.

Table 3 : Significant Contribution of Employment Income to Income Tax Revenue of Nepal

Response	Yes		No		Total	
	No.	%	No.	%	No.	%
Tax experts	60	50	0	0	60	50
Employees	60	50	0	0	60	50
Total	120	100			120	100

Source: *Survey, 2021*

The question was received from all respondents. 100% of total respondents accepted the contribution of remuneration tax significantly to the income tax revenue of Nepal. Thus the conclusion can be drawn that the remuneration tax is contributing significantly to the income tax revenue of Nepal.

b. Major Problem of Soundness and Effectiveness of Remuneration Tax System in Nepal

A supplementary question was asked, "If not, what are the major problems of remuneration tax system?" The opinions of respondents are presented in the following table.

Table 4: Major Problems of Soundness and Effectiveness of Remuneration Tax System in Nepal

S.N.	Problems	Percentage	Rank
1.	Defective Tax rate	17	5
2.	It is high burden of tax on low-level income earners.	18	4
3.	Unfair & weak administration.	22	1
4.	No provision of deducting any expenditure.	19	3
5.	Complexity in income tax policy rules & regulation.	21	2
6.	Other reasons	3	6
	Total	100	

Source: *Survey, 2021*

Table 4 reveals that the main problem of the remuneration tax system of Nepal is unfair & weak administration. The reasons behind the problems of soundness and effectiveness of remuneration tax system are ranked below in order of preference; Unfair & Weak administration, Complexity in income tax policy rules & regulation., No provision of deducting any expenditure, It is high burden of tax on low-level income earners, Defective Tax rate and Other reasons. The respondents said that inappropriate exemption limit and unawareness of the public as other reasons.

c. Reasons behind Low Contribution of Remuneration Tax to Income Tax Revenue of Nepal

To know the reasons behind the low contribution of remuneration tax to income tax revenue of Nepal, the question asked was "In your opinion, what are the reasons behind low contribution of remuneration tax to income tax revenue of Nepal?" The responses received from the respondents are tabulated as below.

Table 5: Reasons behind Low Contribution of Remuneration Tax to Income Tax Revenue of Nepal

S.N.	Alternatives	Percentage	Rank
1.	Low pay scale of the employees.	26	1
2.	Tax evasion.	21	3
3.	Less number of employees having tax liability.	14	5
4.	Ineffectiveness in the implementation of the act.	23	2
5.	Others.	16	4
	Total	100	

Source: *Survey, 2021*

From the table 5, it is clear that the main reason behind the low contribution of remuneration tax to Income tax revenue of Nepal is low pay scale of the employees. The other reasons of the low contribution of remuneration tax are ranked below in order of preference; Low pay scale of the employees, Ineffectiveness in the implementation of the act, Tax evasion, Others, and Less number of employees having tax liability.

In other reasons, most of the respondents said that the lack of proper reward and punishment system for the taxpayer, lack of rebate, concession, facilities to the taxpayers, incapability of the tax administration to find real taxpayers and increase in unemployment rate.

d. Factors to be Initiated to Increase the Contribution of Remuneration Tax in Nepal

To know the factors that increase the contribution of remuneration tax to the income tax revenue of Nepal, the question was asked, "What factors should be initiated to increase the contribution of remuneration tax in Nepal?" The following table shows the rank wise responses received from the respondents.

Table 6: Factors to be Initiated to Increase the Contribution of Remuneration Tax in Nepal

S.N.	Alternatives	Percentage	Rank
1.	Making tax deduction at source (TDS) effective.	22	1
2.	Bringing new taxpayers into tax net.	21	3
3.	Reduction in exemption limit.	16	4
4.	Increasing tax rates.	14	5
5.	Reform in the income tax policy, rules & regulation	21	2
6.	Other	6	6
	Total	100	

Source: *Survey, 2021*

From the table 6, it is clear that the main factor that should be initiated to increase the contribution of remuneration tax in Nepal is making tax deduction at source (TDS) effective. The other factors to be initiated to increase the contribution of remuneration tax in Nepal are ranked below in order of preference; Making tax deduction at source (TDS) effective, Bringing new taxpayers into tax net, Reduction in exemption limit, Increasing tax rates, Reform in the income tax policy, Rules and Regulation and Others.

In other factors the respondents said making self-assessment of tax easier and reliable, provide various facilities to the taxpayers employees and increasing pay scale of the employees.

e. Contribution of Income Tax from Remuneration Tax to the Public Revenue

In order to know whether the contribution of income tax from remuneration tax to the public revenue is effective & satisfactory or not, a question was asked, "Do you think that contribution of income tax from remuneration tax to the public revenue is effective & satisfactory?" The responses received from the respondents are tabulated below.

Table 7: Contribution of Income Tax from Remuneration Tax to the Public Revenue

Respondents	Yes		No		Total	
	No.	%	No.	%	No.	%
Tax Experts	7	6	53	44	60	50
Employees	12	10	48	40	60	50
Total	19	16	101	84	120	100

Source: *Survey, 2021*

From the table 7, it is clear that about 84% of the respondents responded that contribution of income tax from remuneration tax to the public revenue is not effective & satisfactory and only 16 % of the total respondents accepted that the contribution of income tax from remuneration tax to the public revenue is effective & satisfactory.

f. Opinion Towards the Provisions for Deduction of Expenses Required from Remuneration Income

A supplementary question was asked to the respondents to find out their opinions towards the provisions for deduction of expenses required from remuneration income. The question was asked "If not, what types of deductions would you expect to be provided?" The responses received from the respondents are listed below.

Table 8: Opinion Towards the Provisions for Deduction of Expenses Required from Remuneration Income

S.N.	Alternatives	Percentage	Rank
1.	Medical expenses incurred for the treatment of the employee.	19	1
2.	Education expenses and books and reading materials purchased for the job.	15	3
3.	Transportation expenses to go to office and back.	17	2
4.	House rent paid.	12	6
5.	Leave salary.	13	4
6.	Amount received from life insurance.	13	5
7.	Other expenses as of previous Act.	11	7
	Total	100	

Source: *Survey, 2021*

From the table 8, it is clear that the main item for deduction is medical expenses incurred for the treatment of the employee. The different items of deductions suggested by respondents are ranked below in order of preference; Medical expenses incurred for the treatment of the employee, Transportation expenses to go to office and back., Education expenses and books and reading materials purchased for the job, Leave salary., Amount received from life insurance, House rent paid and Other expenses as of previous Act.

g. Problem Faced by Employees While Paying Remuneration Tax

To know the respondents' opinions regarding the problems faced by employees while paying income tax, a question was asked to them. The question was "what types of problem that the employees faced while paying remuneration tax?" The responses received from the respondents are tabulated below.

Table 9: Opinions Towards Some Taxable Incomes to be Made Tax-Exempted

S.N.	Problems	Percentage	Rank
1.	Hesitation to pay income tax due to low income.	15	5
2.	Weak and immature treatment by tax administration.	15	4
3.	Procedural complications.	20	1
4.	Tax personnel discourage giving tax clearance certificate.	19	2
5.	Due to lack of taxation knowledge, employees do not know how to file returns.	18	3
6.	Others	13	6
	Total	100	

Source: *Survey, 2021*

From the table 9, it is found that the most important problem faced by employees while paying remuneration tax is procedural complications. While ranking together the opinions of both the groups, the corresponding prioritized problems are as follows: Procedural complications, Tax personnel discourage giving tax clearance certificate, Due to lack of taxation knowledge, employees do not know how to file returns, Weak and immature treatment by tax administration, Hesitation to pay income tax due to low income and Others.

Discussion

The remuneration tax has significant contribution on total government revenues. Kafle (2019) also found out that inefficiency in the income tax administration is due to cause of government inefficiency. The income tax to GDP, total revenue and direct tax revenue was in increasing trend. The contribution of remuneration tax in total income tax revenue of Nepal has not been found satisfactory due to unfair &

weak administration, complexity in income tax policy rules & regulation, no provision of educating any expenditure, it is high burden of tax on low level income earners. The result is supported by OECD (2021), where focuses in particular on how tax policy can be designed comprehensively so that fiscal systems can deliver a balance of equity, growth and sustainability, highlighting some of the key considerations that policymakers should take into account to ensure optimal tax policy design and the successful implementation of tax reform.

Conclusion and Implications

The remuneration tax has a significant contribution on total government revenues. Remuneration tax has 2% to 20% contribution on total income tax during ten fiscal years. Highest 22% opined unfair and weak administration is found as major problem of remuneration tax. Major facilities and benefits are: highest 24% preferred medical expenses, 23% preferred pension income then remote area allowance. Major facilities and benefits are: highest 24% preferred medical expenses, 23% preferred pension income then remote area allowance. So, medical expenses paid by employer, dashain allowance, etc. should are tax exempted. From the opinion survey conducted towards the tax expert and employees, the conclusion can be drawn out that remuneration tax as a suitable means of collecting government revenue. The contribution of remuneration tax in total income tax revenue of Nepal has not been found satisfactory due to unfair & weak administration, complexity in income tax policy rules & regulation, no provision of educating any expenditure, it is high burden of tax on low level income earners.

The high rate on remuneration tax encourages the evasion, discourages the payment and influences the taxpayers' decision on the financial activities; this is detrimental to both the public authorities and taxpayers or citizen. Good tax policy is one that strives to provide benefit to all the concerned sectors. Thus, it is suggested that the government should make an adequate consultation with all the concerned groups of people and responsible body of the government to determine the policies and programs in order to collect adequate and justifiable tax revenue to make the nation prosper.

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