Tax Compliance and Enforcement Trends in Nepal

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Inland Revenue Department
Outline of the Presentation

- Introduction to the IRD
- Mandate and Approaches
- Revenue Performance
- Challenges Ahead
- Direction to the Future
- Major Compliance Issues
- Legal Provision to Enforcement
- Initiations for Enhancing Compliance
- Major Results Expected
Established in July 2002 after the merger of the Value–Added Tax Department and Income Tax Department

Staffed by approximately 1,000 permanent and 300 contractual staff

Offices—1 LTO, 22 IROs, and 28 TSOs—13 in the valley and 10 outside the valley
Number of Taxpayers

<table>
<thead>
<tr>
<th>Income Tax</th>
<th>PIT</th>
<th>Total</th>
<th>VAT</th>
</tr>
</thead>
<tbody>
<tr>
<td>541,424</td>
<td>232,689</td>
<td>874,113</td>
<td>113,919</td>
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</table>
Mandate

- Income Tax
- VAT
- Excise
- Health Tax
- Education Fee
IRD Approaches to Taxation

- Voluntary compliance-based tax system
- Research-based tax policy reform
- Need-based taxpayer education and awareness
- IT-based taxpayer service
- Scientific forecasting-based revenue estimation
- Indicator-based risk management & audit
- Functional- and segment-based organization
- Information- and intelligence-based enforcement
- Evidence-based tax investigation
- Cadre-based, taxpayer-friendly administration
- Fare-based administrative review system
Composition of Tax Revenue (%)

- Share of Land and Vehicle Ownership
- Share of International Trade based Revenue
- Share of Inland Revenue

<table>
<thead>
<tr>
<th>Year</th>
<th>Land and Vehicle Ownership (%)</th>
<th>International Trade (%)</th>
<th>Inland Revenue (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2011/12</td>
<td>3.78</td>
<td>48.73</td>
<td>47.49</td>
</tr>
<tr>
<td>2010/11</td>
<td>3.93</td>
<td>49.48</td>
<td>46.59</td>
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<tr>
<td>2009/10</td>
<td>6.63</td>
<td>50.55</td>
<td>42.82</td>
</tr>
<tr>
<td>2008/09</td>
<td>7.72</td>
<td>48.53</td>
<td>43.95</td>
</tr>
<tr>
<td>2007/08</td>
<td>5.89</td>
<td>49.69</td>
<td>44.42</td>
</tr>
<tr>
<td>2006/07</td>
<td>5.94</td>
<td>48.72</td>
<td>45.34</td>
</tr>
</tbody>
</table>
### Tax-to-GDP Ratio

- **Domestic Revenue Mobilization**

<table>
<thead>
<tr>
<th>Tax-to-GDP ratio (%)</th>
<th>Nepal</th>
<th>LIC</th>
<th>OECD</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>13.2</td>
<td>15.2</td>
<td>35</td>
</tr>
</tbody>
</table>
People in Tax Net

Population of 28 million

Taxpayers: 0.9 million
Challenges

- Bringing informal economy into tax net
- Cutting down compliance costs
- Detecting tax fraud and action against it
- Keeping up high morale of the tax personnel
- Enhancing professionalism
- Sustainability of e-tax, e-payment, ABBS system, and initiation of TIN
Challenges (cont’d)

- Taxpayer education to all taxpayers
- Creating taxpayer-friendly treatment
- Enhancing voluntary compliance of highly noncompliant behavior.
- Joint collaboration with other agencies (i.e. private sectors, other orgs, etc.)
- Taxing e-commerce
- Knowing your customer (KYC)
Vision—An efficient organization for internal revenue mobilization, professional services, innovation, and economic growth
Mission and Objectives

Mission—Ensuring voluntary tax compliance through quality service and enforcement with fairness

Overall Objective—Improving efficiency and effectiveness in the tax system
IRD Strategic Plan: At a Glance

VISION: An efficient organization for internal revenue mobilization, professional services, innovation and economic growth.

MISSION: Ensuring voluntary tax compliance through quality service and enforcement with fairness.

OVERALL OBJECTIVE: IMPROVING EFFICIENCY AND EFFECTIVENESS IN THE TAX SYSTEM

1. Policy Reform and Enhancement of Enforcement
   1.1 Tax policy reform.
   1.2 Harmonization of tax laws and procedural framework on par with international standards.
   1.3 Operationalization of research and forecasting for maximization of revenue collection.
   1.4 Application of tax information network, enhancement of tax enforcement and risk management.

2. Improving Taxpayer Service and Education
   2.1 Empowering taxpayers on related laws and tax issues through education, counseling and other outreach programs.
   2.2 Increasing voluntary compliance and reduction of compliance cost.
   2.3 Identify and reduce non-compliance.
   2.4 Promote timely reporting and payment of taxes.

3. Optimal Uses of Modern Technology
   3.1 Enhancement of ICT network.
   3.2 Operationalization of full-scale e-governance system.
   3.3 Regular auditing and management of ICT system to international standards.
   3.4 Establishment of professional forward linkage with national and international agencies.

4. Revitalization of the Organization System: Mobilization of Competent Human Resources
   4.1 Transformation of IRD into a competent organization.
   4.2 Increase coverage and access of service for potential taxpayers with low administrative cost.
   4.3 Application of tax cadastral registration system, a professional and compatible HRM policy plan.
   4.4 Revitalization of human resources and capacity building.

VALUES
- Equity
- Valuing People
- Integrity & Commitment
- Collaboration
- Innovation
The Priority Areas for Reform

- Policy and Legislation
- Taxpayer Service
- Enforcement and Compliance
- HR Management
- Budget
- e-Services and IT
- Org. and Mgmt.
Compliance Trend in Return Filing

- 2008/09: 19% (Non filer of VAT) + 45.51% (Non filer of IT)
- 2009/10: 27% (Non filer of VAT) + 41% (Non filer of IT)
- 2010/11: 21.25% (Non filer of VAT) + 51.18% (Non filer of IT)
- 2011/12: 22.30% (Non filer of VAT) + 50.59% (Non filer of IT)
Compliance Pyramid

A New Approach to Tax Compliance

- Prosecution
- Command Regulation (Non-discretionary)
- Command Regulation (Discretionary)
- Enforced Self-regulation
- Self-regulation
- Real Time Business Examinations/Record Keeping Reviews
- Education/Record Keeping/Service Delivery (convenience, access, choice, control)
- Commitment
- Capitulation
- Resistance
- Disengagement
- MOTIVATIONAL POSTURES
- REGULATORY STRATEGIES
- ENFORCEMENT STRATEGIES
Major Compliance Issues

- Low registration (income tax and VAT)
- Low return filing (huge non-filers)
- Under invoicing and non-invoicing
- Data mismatch (difference in reporting)
- Tax fraud (fake VAT bill case)
- Huge amount of tax dues
- Large no. of cases pending in Revenue Tribunal
- No new policy and no new tax rates for the last one year
- No supportive environment for enforcement
Legal Provision to Enforcement

- Monitoring of suspected taxpayers
- Selection of cases for audit and investigation based on risk factors
- Imposition of financial penalties:
  - Additional charges;
  - Fees;
  - Interest;
  - Penalty, etc.
- Suspension of Transaction
- Closure of Business
- Imprisonment
Initiatives for Compliance Enhancement

- Tax system reform year announcement
- Implementation of 5-year strategic plan and 3-year reform plan
- Initiation of organizational restructuring
- Taxpayer segmentation study undergoing
- Human Resources Management Plan prepared
- National Tax Day celebrated for the first time
- Application of service to enforcement strategy
- Communication strategy (use of Tax Bulletin, Radio, TV, News, Print, etc.)
Initiatives for Compliance Enhancement

- Revenue research and forecasting unit established
- Online taxpayer service (call center, etc.)
- Initiation of tax information network (TIN)
- Data link with Company Registrar Office has already been started
- Integrated market monitoring and billing enforcement program
National Tax Day Celebration
Tax Clinic

Government of Nepal
Ministry of Finance
Inland revenue Department

Tax Clinic
प्रथम राष्ट्रिय कर दिवस तथा कर सप्ताह सफलतापूर्वक सम्पन्न
Tax System Reform

Strategy Plan

Reform Plan

IRD in 5 Years

Activities for Next 3 Years
Major Results Expected

- Tax-to-GDP ratio increased to 18% within 5 years
- 100% of large taxpayers and 2% of other taxpayers will be audited annually
- Need-based taxpayer education program
- Maintain non-filer rate below 10% in VAT and 40% in income tax
- Establishment of fully functional and segment-based organization
- Decrease compliance cost by 50%
- Full integration and full automation of VAT, IT, and excise system
Major Expected Results of SP

- Implementation of e-payment system in tax
- Full operationalization of ABBS system for tax collection
- 100% taxpayer registration by online system
- 100% collection of tax returns through e-filing
- Full application of HRM policy
- Reallocation of offices and service units for accessibility of the taxpayers