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Revenue Mobilization and Contribution Patterns in Nepal

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Abstract

The objective of this article is to evaluate the revenue mobilization efforts in Nepal and understand the contribution patterns of various revenue sources. In this article data of gross domestic product (GDP) and total revenue for the fiscal years 2017/18 to 2021/22was collected from publication of IRD of Nepal. It examines key aspects of fiscal federalism, including revenue collection rights, revenue sharing, and intergovernmental fiscal transfers, as governed by the Intergovernmental Fiscal Arrangement Act. The study assesses government revenue as a percentage of GDP, tax revenue efficiency, and the role of the Internal Revenue Department (IRD). It also explores the composition of revenue, distinguishing between tax and non-tax sources. The findings reveal a positive trend in revenue mobilization, with tax revenue playing a significant role. The findings contribute to understanding Nepal's revenue mobilization efforts and the composition of its revenue sources, providing insights into the country's fiscal policies and financial sustainability.

Keywords**:** Revenue mobilization, contribution patterns, GDP, fiscal federalism, tax revenue.

Introduction

In Nepal's federal system, there are primarily three key characteristics of fiscal federalism in terms of revenue mobilization. The first factor is "right to collect the revenue," which is based on the idea of a single tax administration. Therefore, it requires only one government to earn and receive the revenue before distributing it, if any. The second factor is "revenue sharing," which enables governments to allocate a certain sort of revenue among the concerned governments in accordance with regulated legal regulations. The "intergovernmental fiscal transfer" dimension is the third. According to this, the federal government may award funds to all sub-national entities, whilst the province governments may do so at municipal levels within their control.

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The "Intergovernmental Fiscal Arrangement Act, 2017" governs how all three levels of government raise revenue. According to the act, the provincial government can raise money primarily through three non-taxes and five types of taxes.

A nation's economy must be strengthened by increasing government revenue collection. A common issue facing developing nations is a lack of funding for development (Gurtner, 2010). An alternative measure of economic development for developing nations is debt. Government expenditure is financed by debt to support future economic objectives, which may promote economic growth in the future. An economy that is strong at estimating jobs and making savings (Arsyad, 2010; and Kusumasari, 2020).

Eight different types of taxes (wealth tax, house rent tax, house and land registration fee, motor vehicle tax, land tax, entertainment tax, advertisement tax, and business tax) as well as three different types of non-taxes are the primary sources of income for local governments.

Provinces and local governments primarily get funding from revenue sharing and subsidies from the federal government, in addition to tax and non-tax revenue. The value added tax and excise duty earned on domestic goods must be split equally between the provincial and local governments under Nepal's revenue-sharing model, at a rate of 15% each.

As compared to previous years, revenue mobilization in Nepal has been increasing. The ratio of government revenue to GDP increased as well, rising from 14.6 percent in 2009/2010 to 20.3 percent in 2019/2020. Government spending, however, exceeds government earnings. The amount spent by the government was Rs. 250.81 billion in 2009/10; this amount climbed fourfold to Rs. 1038.02 billion in 2019/20. The ratio of government spending to GDP increased from 21.6 percent in 2009/10 to 27.9 percent in 2019/20 (NRB, 2021). With the introduction of federalism, the size of government revenue and expenditure increased.

The goal of social welfare is to provide a community with a range of social, material, and spiritual resources, such as morality, inner and outer peace, and security so that each member can work hard to meet their own needs and meet the needs of their families, society, and themselves. Imron (2012) found that social welfare is synonymous with the well-being of individuals.

In the context of public revenue, contribution patterns typically refer to how taxes are burdened and where money comes from. Depending on their wealth, consumption habits, or income levels, many social groupings make contributions to the public funds. The distribution of the tax burden among various income or wealth levels will determine whether the contribution patterns are progressive, regressive, or proportionate.

The objective of this article is to conduct an in-depth evaluation of Nepal's revenue mobilization efforts. It seeks to gain insights into the patterns of contribution from various revenue sources within the country. The study aims to assess how effectively taxes are being collected within Nepal. Second aspect of the analysis is the examination of the role played by the Internal Revenue Department (IRD) in the process of revenue generation. The final aspect of research is to analyze the composition of Nepal's revenue streams.

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Literature Review

Government revenue is a problem for decision-makers. In emerging nations, where there is a greater demand for funding for development, government revenue is more important. Developing nations would need to rely heavily on local revenue mobilization because an excessive reliance on foreign funding could eventually result in debt sustainability issues and a never-ending debt trap cycle (Gupta, 2007).

There is a direct correlation between public revenue and government development efforts activities of the government. Revenue includes all sources of income for the government, including taxes, fees, fines, duties, penalties, rents, dues, profits, and other types of government receipts for which the legislature has the authority to appropriate funds (Edogbanya and Ja'afaru,2013). According to Arnold and McIntyre (2002), a tax is an enforced charge imposed by the relevant regulations on income, consumption, and the production of goods and services. A tax is a fee imposed by the government on goods, people, or transactions to generate revenue for the general welfare.

According to scientific research, the employment of different fiscal regulation tools to raise general government revenue helps to lessen macroeconomic variable uncertainty and ensure that these variables are properly formed. In light of the sharp declines in commodity prices, the general government must first implement modest adjustments to its fiscal regulation system to raise the necessary funds for citizen welfare (Lopez-Martin, Leal, & Fritscher, 2019).

In order to boost public spending to meet public needs and to create revenue stability in the face of uncertainty and risk, income diversification has been regarded as one of the key funding techniques (Martin et al., 2012; Carroll, 2009). For macroeconomic stability to be maintained, the growth in tax income must approximately match the growth in spending (World Bank, 1990).

To ensure fiscal sustainability and the effectiveness of the fiscal regulation system to produce general government revenue, fiscal strategies based on revenue generation modeling are to be established. Macroeconomic stability is found to be facilitated by efficient fiscal policy that is based on long-term projections of general government revenue collection and public finance utilization (Agenor, 2016). To maintain the sustainability of public finances and promote interregional factor mobility, it is crucial to justify the ideal level of tax burden, including tax rates, against the backdrop of capital tax. When there are no differences, it makes sense that greater capital flows between nations boost economic growth and raise the level of fiscal sustainability across the board. However, when there are notable differences, tax competition brought on by capital flows may lower the fiscal sustainability across the board. However, when there are notable differences, tax competition brought on by capital flows may lower the fiscal sustainability in a nation with substantial capital and a high percentage of outstanding debt (Miyazawa et al., 2019).

It critically engages with the existing body of scholarly work focused on delineating the factors that wield influence over the establishment of good governance in developing nations, with a specific emphasis on the realm of local governments. Broadly, the discussion seeks to unravel the intricate tapestry of variables and dynamics that shape the landscape of governance, shedding light on their implications for developmental trajectories. The significance of this inquiry is underscored by the prevailing challenges faced by the majority of low-income nations, where insufficient provision of public goods poses formidable obstacles to progress. Within this context, understanding the

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determinants of good governance becomes a matter of paramount importance, serving as a linchpin for addressing the developmental barriers intrinsic to these nations. The insights encapsulated in this review draw upon the seminal works of the World Bank (2004) and Besley and Ghatak (2006). By synthesizing findings from these key sources, the literature review aims to contribute to a nuanced comprehension of the intricate nexus between influencing factors, good governance, and the unique challenges faced by developing nations, particularly within the purview of local governance structures.

The study critically evaluates the efficacy of initiatives aimed at mobilizing funds, dissecting the intricate patterns of contribution emanating from various revenue sources. The research specifically directs attention to the federal system in Nepal, serving as a comparative touchstone. Through a meticulous analysis of the successes and challenges encountered by emerging nations, the review endeavors to contribute valuable insights to our collective understanding of fiscal decentralization. The overarching goal is to discern the impact of these fiscal strategies on economic growth within a broader context. The findings encapsulated in this review furnish a valuable addition to the reservoir of knowledge surrounding the effects of fiscal decentralization on economic growth. By scrutinizing the experiences of diverse nations and drawing pertinent comparisons with the federal system of Nepal, this literature review aims to enrich our comprehension of the intricate interplay between fiscal federalism and broader economic dynamics (Smith et al., 2019).

Garcia et al. (2020) aim to clarify the complex relationship between economic growth and taxation policy by examining the varied effects of tax schemes on revenue collection in emerging nations. This writing carefully explores the empirical field, breaking down the complex network of economic complexities. The main focus of the study is on how tax policies affect revenue generation in developing countries, specifically examining the consequential implications of such policies. Through a critical lens, the intricate workings of Nepal's budgeting strategies are revealed. Based on a careful examination of actual data, the writers reveal the complex effects of current tax policies on Nepal's economy. The academic discussion includes a thorough assessment of the current situation as well as thoughtful suggestions for strengthening and improving tax arrangements. The ultimate objective is to spark long-term, sustainable financial growth in a setting of development. This literature study adds to the body of knowledge by providing a comprehensive understanding of the relationship between economic growth, revenue mobilization, and taxation policies. It also has practical consequences for stakeholders and policymakers in the developing economy.

This paper provides a thorough analysis of Nepal's revenue mobilization efforts and briefly notes changes in the GDP-to-total revenue and GDP-to-tax revenue ratios, which may indicate changes in the effectiveness of tax collecting. The importance of efficient fiscal policies in preserving macroeconomic stability is touched upon in passing. These issues were not fully investigated in earlier research; for this reason, this article attempts to fill in the gaps. Even though the Internal Revenue Department (IRD) plays a crucial role in revenue collection, more research might be done to examine particular elements that affect the IRD's effectiveness. This investigation can include a review of technology interventions, administrative procedures, and capacity-building initiatives.

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Research Methodology

Regarding the methodology used, the research is classified as descriptive in nature. It relies entirely on secondary data sources. To gather the necessary information, data related to Gross Domestic Product (GDP) and total revenue for the fiscal years 2017/18 to 2021/22was collected from publications made available by the Internal Revenue Department (IRD) of Nepal. Similarly, data regarding the revenue structure in the fiscal year 2021/22 were obtained from publications released by the IRD. In short, this article adopts a descriptive research approach to provide a comprehensive assessment of Nepal's revenue mobilization. It draws on secondary data sources to analyze the effectiveness of tax collection, the role of the IRD, and the overall composition of revenue in the country, with a focus on tax and non-tax revenue sources. These insights aim to contribute to a better understanding of Nepal's fiscal policies and its financial sustainability.

ANALYSIS AND DISCUSSION

Revenue mobilization efforts in Nepal, contribution patterns of various revenue sources and revenue structures are analyzed under below.

The ratio of revenue mobilization to the total Gross Domestic Product (GDP) is a crucial economic indicator that reflects a country's ability to generate revenue from various sources in relation to its overall economic output. This ratio is often used to assess a government's fiscal performance and its capacity to fund public services, infrastructure, and other essential expenditures. Ratio of revenue mobilization with total GDP for the fiscal years 2017/18 to 2021/22 is presented with the help of following table.

Table 1: Ratio of Revenue Mobilization with Total Gross Domestic Product

Fiscal Year	2017//18	2018/19	2019/20	2020/21	2021/22
Gross Domestic Product	3455.95	3858.93	3914.7	4266.32	4851.62
Total Revenue	726.72	829.63	793.75	938.32	1067.96
Gross Domestic Product/ Total Revenue (in %)	21.03	21.50	20.28	21.99	22.01
Tax Revenue	659.49	738.6	700.05	870.11	984.16
Gross Domestic Product/ Tax Revenue (in %)	19.08	19.14	17.88	20.39	20.29

Source: (IRD, 2021/22)

Table 1 portray that the ratio of GDP to total revenue was 21.03% during the fiscal year 2017/2018. The ratio grew to 21.50% in the fiscal year 2018/2019, reflecting a little stronger revenue mobilization than the GDP. The ratio fell to 20.28% in the fiscal year 2019/20, reflecting a lower share of revenues collected in relation to the GDP. The ratio increased once again to 21.99% during the fiscal year 2020/2021, indicating a rise in revenue mobilization relative to GDP. The ratio held steady at 22.01% for the fiscal year 2021/22.

On the other side, the GDP to tax revenue ratio evaluates the effectiveness of taxation. It displays the percentage of tax revenue collected in relation to the GDP. The GDP to tax revenue ratio was 19.08%

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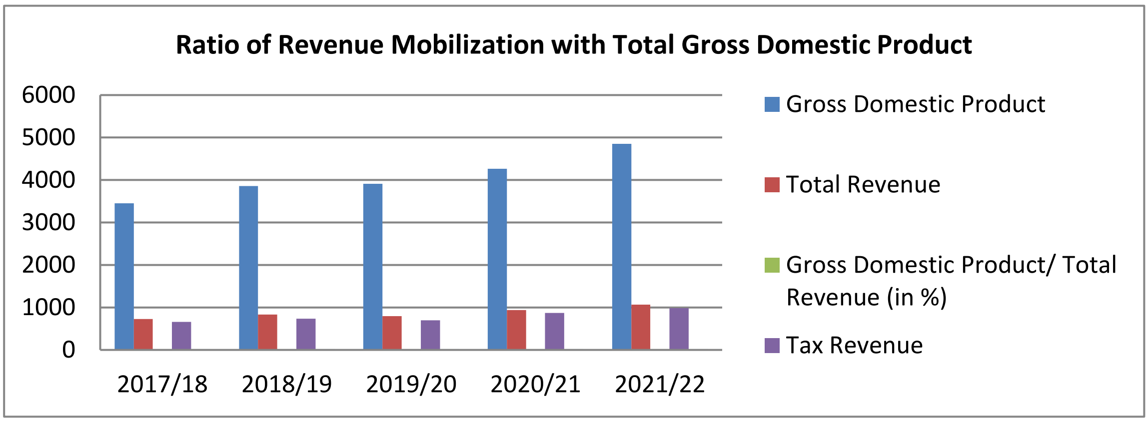
in 2017/18. The rates range from 19.14% to 20.39% in the later years. Higher ratios reflect more effective tax collection, resulting in higher tax revenue as a percentage of GDP.

Above ratios show that government efficiency has not increased remarkably the effectiveness of tax collection during the five fiscal years. This ratio makes it possible to comprehend how well the government is able to raise money and how well the economy is taxed. Ratio of revenue mobilization with total gross domestic product is presented with the help of following figure.

Figure 1: Ratio of Revenue Mobilization with Total Gross Domestic product



Excise duty, income tax, and value added tax (VAT) are the major sources of income of the government and their ratio to the Gross Domestic Product (GDP) for the fiscal years 2017/18 to 2021/22 is presented with the help of following table.

Table 2: Ratio of Excise Duty, Income Tax and VAT with Total Gross Domestic Product

Fiscal Year	2017//18	2018/19	2019/20	2020/21	2021/22
Ratio of Excise to GDP	2.97	3.16	2.65	3.14	3.44
Ratio of Income Tax to GDP	4.63	5.04	5.61	5.39	5.36
Ratio of VAT to GDP	5.98	6.22	5.72	6.61	6.48

Source: (IRD, 2021/22)

In Table 2, the ratio of Excise Duty to GDP in the fiscal year 2017/18 is 2.97% and this ratio rises and becomes 3.44% in the fiscal year 2021/22. This ratio is rising except for the fiscal year 2019/20. A higher ratio indicates a larger share of the GDP being contributed by Excise Duty revenue.

The ratio of Income Tax to GDP measures the proportion of Income Tax revenue collected in relation to the size of the GDP. In 2017/18, the ratio of income tax to GDP is 4.63% and this ratio rises and becomes 5.36% in the fiscal year 2021/22. But this ratio is not increasing satisfactory level as compared to other countries. A higher ratio suggests that a larger share of the GDP is generated through Income tax revenue.

The ratio of VAT to GDP measures the proportion of VAT revenue collected in relation to the size of the GDP. In 2017/18, the ratio of VAT to GDP is 5.98% and this ratio rises and becomes 6.61% in the fiscal year 2021/22. A higher ratio indicates a larger share of the GDP being contributed by VAT revenue.

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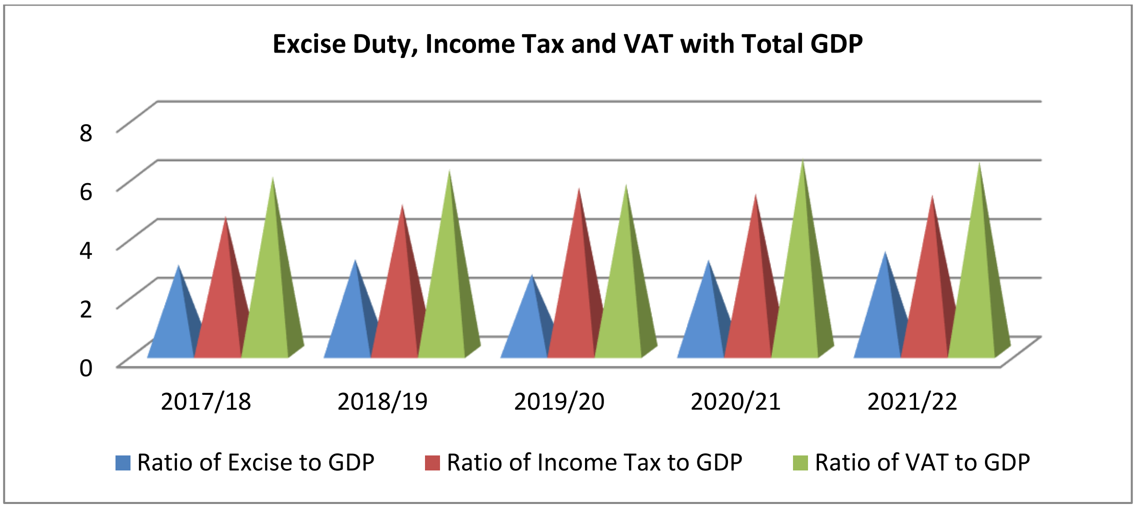
These ratios provide insights into the contribution of Excise Duty, Income Tax, and VAT to the overall revenue generated in the economy relative to the size of the GDP. But VAT contribution is more than exercise duty and income tax. Ratio of excise duty, income tax and VAT with total gross domestic product is presented with the help of following figure.

Figure 1: Excise Duty, Income Tax and total GDP



To generate revenue for the government, Internal Revenue Department's (IRD) role is very crucial. There is a positive relationship between IRD's efficiency and the internal revenue of the government. Hence government should give more attention to well equip this department. The contribution of the internal revenue department to the collection of total revenue for the fiscal years 2017/18 to 2021/22 is presented with the help of the following table.

Table 3: Contribution of the Internal Revenue Department to the Collection of Total Revenue

Fiscal Year	2017//18	2018/19	2019/20	2020/21	2021/22
Total Revenue (bn.)	726.72	829.63	793.75	938.32	1067.96
IRD's Collection (bn.)	298.73	358.36	384.42	429.12	483.48
Share %	41.11	43.20	48.43	45.73	45.27

Source: (IRD, 2021/22)

Table 3 displays the contribution of the Internal Revenue Department's (IRD) to the collection of total revenue for the fiscal years 2017/18 to 2021/22. In 2017/18, the total revenue collected was 726.72 billion units (bn). Out of this, the IRD's collection amounted to 298.73 bn. In 2018/19, the total revenue increased to 829.63 bn, and the IRD's collection also increased to 358.36 bn. The IRD's share of the total revenue rose to approximately 43.20%. For the fiscal year 2019/20, the total revenue decreased to 793.75 bn, but the IRD's collection increased to 384.42 bn. As a result, the IRD's share of the total revenue significantly increased to approximately 48.43%. In 2020/21, the total revenue further increased to 938.32 bn, while the IRD's collection amounted to 429.12 bn. The IRD's share of the total revenue decreased slightly to approximately 45.73%. Finally, in 2021/22, the total revenue reached 1067.96 bn, and the IRD's collection amounted to 483.48 bn. The IRD's share of the total revenue remained relatively stable at approximately 45.27%.

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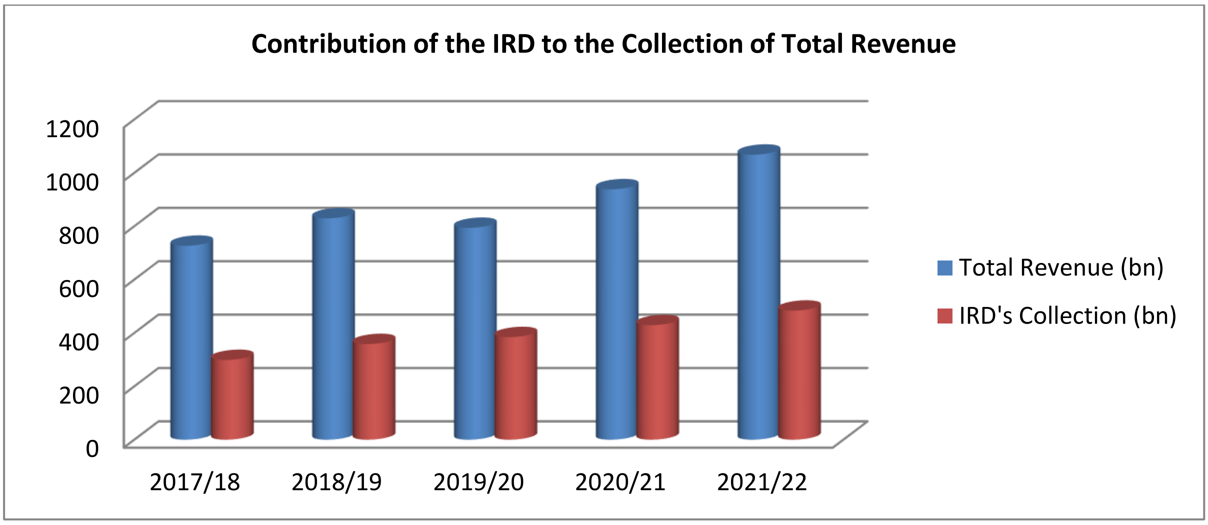
These figures provide an understanding of the contribution of the Internal Revenue Department to the overall collection of total revenue. The IRD plays a significant role in revenue generation, with its share varying between 41.11% and 48.43% over the specified fiscal years. It highlights the importance of the IRD's efforts in collecting revenue for the government's budget and fiscal operations. Contribution of the IRD to the collection of total revenue is presented with the help of following figure.

Figure 3: Contribution of the IRD to the Collection of Total Revenue



The income collected by the government from different sources is called government revenue. It plays a very important role in economic growth and development. Normally, government revenue is classified into tax revenue and non-tax revenue which helps us to understand the composition of the government's revenue sources. Tax revenue typically forms a major portion of the total revenue, while non-tax revenue contributes a smaller portion. This revenue structure is important for analyzing the government's fiscal policies, revenue mobilization efforts, and the overall financial sustainability of the country. The structural contribution of revenue of the government for the fiscal year 2021/22 is presented with the help of the following table.

Table 4: Structural Contribution of Revenue of Fiscal Year 2021/22

Types of Revenue	Amount (in Arab)
Tax Revenue	984.16
Non-Tax Revenue	83.79
Total Revenue	1067.95

Source: (IRD, 2021/22)

Table 4 display that tax revenue amounted to 984.16 Arab. Tax revenue is generated through various taxes imposed by the government, such as income tax, value-added tax (VAT), excise duty, customs duty, and others. It represents the portion of revenue collected directly from individuals, businesses, and other entities based on their taxable activities and income. Non-tax revenue amounted to 83.79 Arab. Non-tax revenue refers to the revenue generated by the government from sources other than taxes. This includes various sources such as fees, fines, penalties, royalties, dividends, profits from state-owned enterprises, grants, and other forms of income. The total revenue collected in fiscal year

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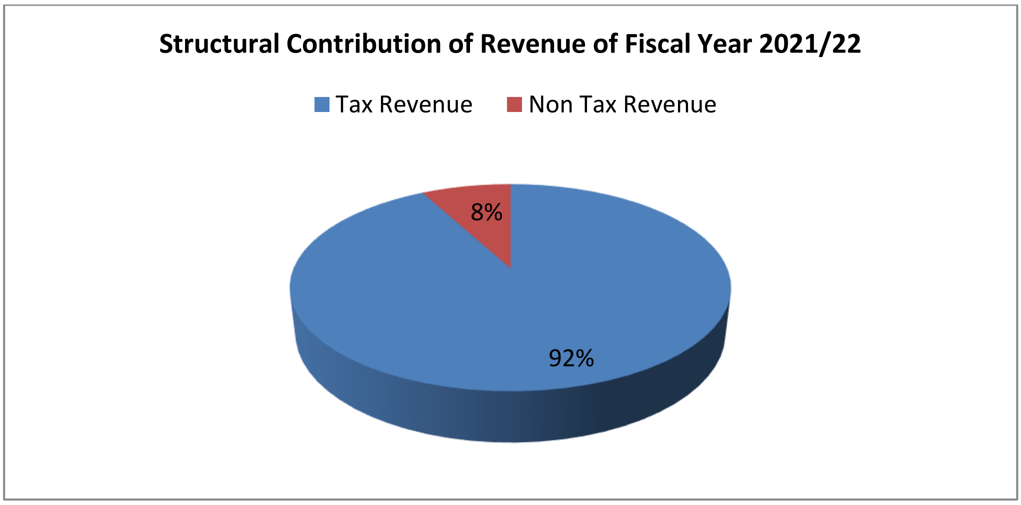
2021/22 was 1067.95 Arab, which includes both tax revenue and non-tax revenue. Share of tax revenue contribution is about 92% and non-tax contribution is only about 8% in the fiscal year 2021/22.Structural contribution of revenue of fiscal year 2021/22 is presented with the help of following figure.

Figure 4: Structural Contribution of Revenue of Fiscal Year 2021/22



A source of revenue collection is categorized into tax revenue and non-tax revenue. Major heading sources of public revenue of the government for the fiscal year 2021/22 are presented in the following table.

Table 5: Sources of Revenue Collections in Fiscal Year 2021/22

Types of Revenue	Amount (Rs. in Arab)
Custom Income	241.78
VAT	314.27
Excise revenue	166.77
Income Tax	260.08
Other Tax	1.26
Total Tax Revenue	984.16
Non Tax Revenue	83.79
Total Revenue	1067.95

Source: (IRD, 2021/22)

Table 5 displays the income sources of government in the fiscal year2021/22. Custom income generated Rs. 241.78 Arab. This revenue is collected from import duties, export duties, and other charges levied on goods and services crossing the country's borders. VAT contributed Rs. 314.27 Arab to the total revenue. VAT is a consumption-based tax imposed on the value added at each stage of the supply chain and is generally levied on the sale of goods and services.

Excise revenue contributed to Rs. 166.77 Arab to the total revenue. Excise revenue is a tax imposed on specific goods and services such as alcohol, tobacco, petroleum products, luxury goods, and certain services. Income tax collections reached Rs. 260.08 Arab. Income tax is a tax levied on the income

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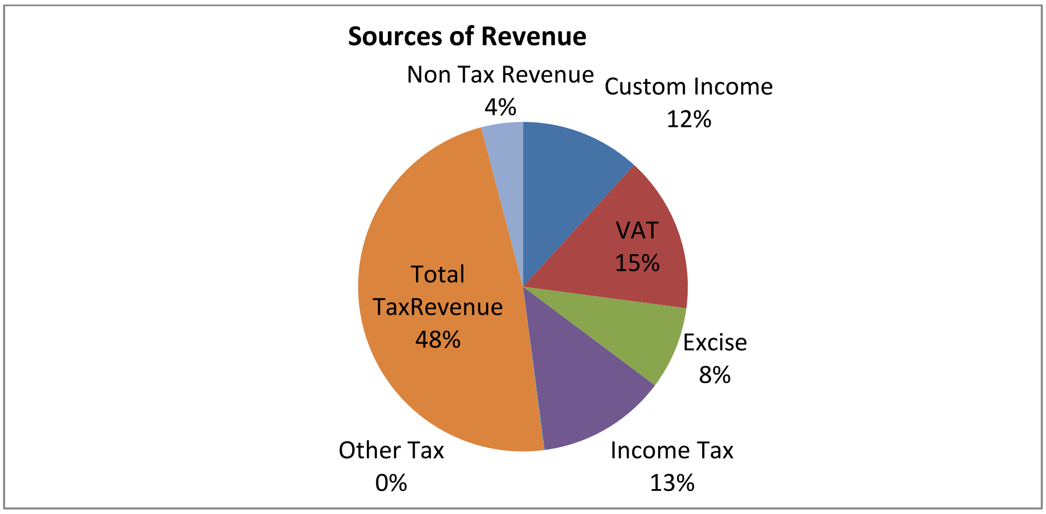
earned by individuals, businesses, and other entities, typically based on their taxable income. Other tax revenue accounted for Rs. 1.26 Arab. This category may include various specific taxes imposed by the government. The total tax revenue collected in fiscal year 2021/22 was Rs. 984.16 Arab. Tax revenue is a significant source of income for the government, and the distribution among different tax types reflects the contribution of various economic activities and tax policies.

Additionally, non-tax revenue contributed Rs. 83.79 Arab to the total revenue. Non-tax revenue comprises various sources such as fees, fines, penalties, dividends, profits from state-owned enterprises, grants, and other forms of income not directly related to taxation. The total revenue collected in fiscal year 2021/22, combining tax revenue and non-tax revenue, amounted to Rs. 1067.95 Arab. The composition of revenue from different sources helps to analyze the government's revenue structure and the reliance on different revenue streams to fund public expenditures and meet financial obligations. A source of revenue collections in fiscal year 2021/22 is presented with the help of following figure.

Figure 5: Sources of Revenue Collections in Fiscal Year 2021/22



Conclusion and Implementation

Nepal's fiscal federal system is characterized by the right to collect revenue, revenue sharing, and intergovernmental fiscal transfers. The Intergovernmental Fiscal Arrangement Act, of 2017, governs how the three levels of government raise revenue, with provinces having specific sources for revenue generation. Revenue mobilization in Nepal has been increasing over the years, with the government revenue-to-GDP ratio rising from 14.6% in 2009/2010 to 20.3% in 2019/2020. Government spending has also increased significantly, leading to a widening gap between revenue and expenditure. Eight different types of taxes and three types of non-taxes constitute the primary sources of income for local governments in Nepal. Provinces and local governments receive funding from revenue sharing and subsidies from the federal government, in addition to tax and non-tax revenue. Nepal faces economic challenges, including a widening resource gap, increasing government expenditure, and a high reliance on foreign aid. Debt sustainability issues and a growing foreign debt burden pose risks to the country's economic stability. Tax revenue forms a major portion of the total revenue, contributing around 92%, while non-tax revenue contributes around 8%. Major tax sources include custom income, VAT, excise revenue, income tax, and other taxes, reflecting the diverse sources of government income. The IRD plays a crucial role in revenue generation, contributing between 41.11% and 48.43% of the total revenue over the specified fiscal years. The ratio of GDP to total revenue and GDP to tax revenue provides insights into the efficiency of tax collection. The ratios have shown variations, indicating room for improvement.

The government's ability to generate revenue relative to the GDP has fluctuated over the years, with the ratio ranging from 20.28% to 22.01% in recent fiscal years. Efficient fiscal policies, based on long-term projections of general government revenue collection, are crucial for maintaining macroeconomic stability and fiscal sustainability. Nepal's economic performance and fiscal challenges necessitate a careful balance between revenue generation and expenditure. Diversification of income sources and attention to fiscal sustainability are recommended to address economic challenges.

The implementation of the findings and insights from this article on revenue mobilization and contribution patterns in Nepal holds significant implications for the country's fiscal policies and financial sustainability. To enhance revenue mobilization, the government should continue to focus on strengthening the effectiveness of tax collection, particularly by improving income tax and excise duty collection mechanisms. Additionally, it should prioritize the development and capacity building of the Internal Revenue Department (IRD) to ensure its continued pivotal role in revenue generation. Furthermore, diversifying revenue sources beyond taxation should be explored, with an emphasis on increasing non-tax revenue streams and exploring innovative income sources to support public spending and mitigate the challenges posed by escalating government expenditures. This article underscores the importance of sound fiscal management and prudent financial policies in Nepal's federal system, ultimately contributing to the nation's economic development and stability.

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