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# Contents

<table>
<thead>
<tr>
<th>Section</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>Editorial</td>
<td>2</td>
</tr>
<tr>
<td>President's Message</td>
<td>3</td>
</tr>
<tr>
<td><strong>Taxation</strong></td>
<td></td>
</tr>
<tr>
<td>IAS/NAS 12 Income Taxes – A Brief Analysis</td>
<td>7</td>
</tr>
<tr>
<td>- CA. Surya Bhakta Pokharel</td>
<td></td>
</tr>
<tr>
<td>- CA. Bishnu Prasad Bhandari</td>
<td></td>
</tr>
<tr>
<td>Considerations for Tax Audit</td>
<td>16</td>
</tr>
<tr>
<td>- Mr. Ramu Prasad Dotel</td>
<td></td>
</tr>
<tr>
<td>Impact of Tax Concession in Foreign Investment</td>
<td>21</td>
</tr>
<tr>
<td>- CA. Bhava Nath Dahal</td>
<td></td>
</tr>
<tr>
<td>Tax Exemptions and Concessions: An Overview</td>
<td>25</td>
</tr>
<tr>
<td>- CA. Prabin Raj Kafie</td>
<td></td>
</tr>
<tr>
<td>Capital Gain Tax a Big Surprise to Many</td>
<td>31</td>
</tr>
<tr>
<td>- CA. Arun Raut</td>
<td></td>
</tr>
<tr>
<td>Tax Buoyancy and Elasticity</td>
<td>36</td>
</tr>
<tr>
<td>- CA. Ananda Shrestha</td>
<td></td>
</tr>
<tr>
<td>Double Taxation Avoidance Agreement (DTAA)</td>
<td>40</td>
</tr>
<tr>
<td>- CA. Gaurav Shrestha</td>
<td></td>
</tr>
<tr>
<td>Taxing Mergers &amp; Acquisitions in Nepal</td>
<td>48</td>
</tr>
<tr>
<td>- CA. Nil Saru</td>
<td></td>
</tr>
<tr>
<td>Corporate Tax Planning through Use of Losses</td>
<td>54</td>
</tr>
<tr>
<td>- Ms. Anupama Ghimire</td>
<td></td>
</tr>
<tr>
<td><strong>News</strong></td>
<td>58</td>
</tr>
<tr>
<td><strong>Notices</strong></td>
<td>15, 35, 47</td>
</tr>
<tr>
<td><strong>Contribution</strong></td>
<td></td>
</tr>
<tr>
<td>Himalayan Bank Ltd.</td>
<td></td>
</tr>
<tr>
<td>Sipradi Trading Pvt. Ltd.</td>
<td></td>
</tr>
<tr>
<td>Employees Provident fund</td>
<td></td>
</tr>
<tr>
<td>Nepal Telecom</td>
<td></td>
</tr>
<tr>
<td>Prabhu Bank</td>
<td></td>
</tr>
</tbody>
</table>
To keep the pace with the growing development expenditure, the government mobilizes resources by way of revenue collection under various Acts. Therefore, taxation has always become matters of discussion every year when the government tables the budget in the Parliament because the tax policy impacts every people of the country. In the efforts to publish special issue of the Journal, the Editorial Board decided to publish a special issue on taxation and requested eminent persons to contribute article for special issue.

The articles in this issue covers divergent aspects of taxation in our country that include applicability of IFRS/NFRS in computation of income tax covering the areas of deferred taxes, fair value presentation, provision of taxation with potential impact on deferred taxes; international tax system to tackle tax avoidance – Base Erosion and Profit Shifting (BEP); tax buoyancy and elasticity with analysis of country situation; impact of tax concessions in foreign investment with critical analysis and challenges facing the country in attracting foreign investment; application of capital gain tax and its TDS mechanism; enforcement of tax legislation with respect to tax exemption and concessions etc. These topics are very much pertinent to the tax authorities and taxpayers. Similarly, these are very useful to the tax consultants also in rendering their tax services.

The authors in their articles have expressed their views that strong political commitment, system based revenue regime and demonstration of ethical behavior by the tax authorities, taxpayers and tax consultants the revenue generation would drastically increase and adequate resources available for developmental works of the government. It is worth to note that the tax consultancy is a highly specialized job because tax laws are not only very complex but also changing very fast. In this context, the members of the Institute are always committed to support to the government honestly by providing efficient and qualitative tax services to the taxpayers based on the prevailing fiscal laws and prevent leakages, wastages and fraud in revenues.
Dear Colleagues,

Last year, I was honored to lead the Institute for a period of one year and my tenure as President of The Institute is towards completion. In the capacity of President of the Institute, this is my fourth and final message to all the membership and stakeholders. During my tenure, I made possible efforts honestly for the development of the Institute and leave this matter to the members and stakeholders for evaluating my performance as President. As a part of my responsibility, I would like to share some major activities that have been performed by the Institute during April to June 2016.

**Student and Education Plan**

The attraction towards chartered accountancy course is growing among the students because of increased market demand and better future career prospects.

As a part of marketing in the chartered accountancy education the Institute has conducted career counseling programs in different places in the country where a large number of the students actively participated in the events. Similarly, the Institute organized 2nd ICAN Career expo, 2016 in Kathmandu. The Institute also participated in Kantipur Hissan Career Fair, 2073 organized in Kathmandu. Likewise, the Institute also organized career seminar in Pokhara, Butwal, Nepalgunj and Biratnagar in order to provide the information about CA education and its future prospects.

The Institute regularly revises the courses of chartered accountancy education to provide greater advantages to the students. The Institute revised all course books of CAP II level and course books of CAP III level is still in the revision process and will be completed soon.

The Institute has made the mandatory provision of one year internship to foreign CA qualification holders pursuant to Rule 41(Kha) of Nepal Chartered Accountants Regulation, 2004, for strengthening their capacity in the field of profession.

For the purpose of measuring the eligibility of the students studying in the CA courses, the Institute during April 1 to June 30, 2016 conducted 13 hall tests in which 5792 students appeared in the tests.

The Institute conducted crash course for CAP III level students to facilitate them for final examination. In the 10 days of crash
course, the Institute provided the guidelines on Advance Accounting, Advance Taxation, Advance Audit and Laws.

As a part of the chartered accountancy curriculum, the Institute conducted general management and communication skills training for CAP III and AT students in ICAN premises for raising their awareness in the field of management and communication as per emerging the market requirements.

In order to improve the students’ affairs of the Institute, we arranged interaction with the representatives of the Students Union, Election Committee members and newly elected president of student union (NCASA).

The Institute has successfully conducted the Final examination of CAP I, CAP II and CAP III Level of June 2016 examination in Kathmandu, Pokhara, Birgunj and Biratnagar including membership examination.

The result of the accounting technician (AT) examination held in March 2016 has been published on 12 May, 2016. According to the results, 3 AT students declared pass out of 12 students appeared in the examination.

Membership and Professional Capacity
In order to update the knowledge of members and assisting them in carrying out their work performance with the changing environment based on the professional and technical standards, the Institute is always playing positive roles in this regard. The contribution of our members in the field of accounting, auditing and other related matters remained satisfactory although there is always room for the improvement.

NFRS implementation is challenging in public and private sectors organizations in the country. With this in view, the Institute has conducted trainings and seminars for members in time to time at different places to disseminate the knowledge in NFRS. During April to June, 2016 the Institute has successfully conducted NFRS training on Chitwan, Nepalgunj, Pokhara and Itahari.

The Institute has published the results of RA upgrading scheme based on file evaluation of RA members in which 1 RA member from D to C class. Similarly RA. Member COP upgrading written examination was conducted in June 2016 in which only one candidate appeared in the examination.

We have established the system to publish the names of newly enrolled chartered accountants in our quarterly journal who have obtained membership of the Institute. I hope that it will be useful to the general public to know about the status of chartered accountant.

Institutional Development
Despite the resource constraints, the Institute is always trying its best in carrying out its activities for the overall development of the Institute. In this connection, the Institute organized various capacity development programs for its members, interaction with students’ representatives, initiated dialogue with different organizations and participated in various programs organized by other organizations. I would like to share some highlights of the programs organized and participated in brief.

The Institute organized a Conference on “Emerging Issues in Accounting Profession “on 27 May, 2016 (Jestha 14, 2073) at Kathmandu and focused on emerging and drivers for Cloud Computing, technical and outsourcing challenges from Business/Client perspective preparing auditors in the areas of cloud - governance, risk and Assurance frameworks based on Global standards and frameworks, as well as other Contemporary Issues in Accounting Profession including Forensic Audit. The Conference also highlighted ethical requirements on marketing & publicity of professional accountants & networking of the firms.

Contemporary Issue Discussion Committee of the Institute organized half day workshop on Anti- Money Laundering (AML) on April 22, 2016 in Kathmandu. During the program two papers were presented related to AML.

In association with the Institute of Chartered Accountants of Nepal, Money Laundering Department organized an interaction program on” Role of Non-financial Professionals on Anti Money Laundering” on 9 May 2016. In the program, the role of auditor is widely discussed in effective implementation of AML.
The ICAN representatives participated in a workshop on the Report on Observance of Standards and Codes—Accounting and Auditing (ROSC-AA) organized by the World Bank in Kathmandu on 22 June 2016 in which I co-chaired the workshop.

**International Relation**

The Institute is always committed to maintain good relation with the International and Regional Accounting bodies for maintaining institutional dignity and to meet the changing professional requirement of IFAC for adaptability and discharging evolving role of the accounting professional. As usual, our representative attended in SAFA Board and Committee Meetings. Similarly, we also participated in SAFA-IFAC Regional PAIB Forum in India, Mumbai held on 9-12 April, 2016.

Our delegation participated in my leadership in CAPA AGM, CAPA Board Meeting and FRED 2 Conference in Kuala Lumpur, Malaysia on 16-19 April, 2016. I believe such kind of visit and participation remained useful in enhancing the capacity of the institute through exchange of practical knowledge and exposures.

The election of the new President of the Council for 2073/74 is approaching and it will be my privilege to hand over the leadership of the Institute to the newly elected President.

Finally, I wish to place on record my sincere gratitude to the council members, committee members, various government authorities, past presidents, students and other stakeholders for their cooperation that helped me in serving the Institute. I also express my thanks to the management team and entire staff for their contribution in discharging my responsibilities. I am pledged to support the Institute and leadership for development efforts for the cause of the profession in the days to come.

Thank you.

CA. Prakash Lamsal
President
सुरक्षित भविष्यको लागि सञ्चयकोष

कोषालाई सञ्चयकर्तालाई उपलब्ध सेवाहरु:

(क) सन्न्य सरकार आयुज्याद : यात्रको यात्राको 6.75 प्रतिशत (२०७२ क्रान्तिका० गतेिेखि)

(ख) सापटी सुविधाहरु:
- विशेष सापटी : ओपेकढीवाँतमाजमाधिमाहिको रकमको १० प्रतिशततर्फ, प्रत्येक वर्ष नवीकरण हुने,
  व्याजदर ५.२५ प्रतिशत।
- घर सापटी : घर निर्माण वा घर/अपार्टमेंट खरीद गर्न:
  सेवाअधिवारवारीधि १० वर्षभन्दा क्षमता एम.ए.भएमा.१२वर्षको तलब वर्षाको रकम,
  सेवाअधिवारवारीधि १० वर्षा सोभानाबादीभएमा १५वर्षको तलब वर्षाको रकम,
  सापटीको अधिकतम सीमा र.१ करोड, व्याजदर ५.२५ प्रतिशत।
- शैक्षिक अनु : घर जगाको धितोमा सञ्चयकर्तालाई बालिको श्रीमान/श्रीमती/ छोरा/छोरीको उच्चविद्यालयात्मक गर्न:
  स्वयंसेवाकलाकारवारीधिमनमूल १० लाख
  विदेशकलाकारवारीधिमनमूल २० लाखसम्म तर ए.मी.सी.एस./ए.मी.डी.को लागि र.५५ लाख सम्म,
  व्याजदर ५.२५ प्रतिशत।
- सञ्चयकर्तालाई सर्विस चुकाउने : घर जगाको धितोमा सञ्चयकर्तालाई ५ लाख र अधिकतम र.१०वर्षको तलब वर्षाको रकम वा र.३० लाखमा जुनकम हुनु भन्ने सो वर्षाको रकम, व्याजदर ६ प्रतिशत।

(ग) सामाजिक सुरक्षा सुविधाहरु:
- दुईघटका मुक्तिपर्व योजना : सेवाकलाका सञ्चयकर्ताको दुईघटकामा परिधमू भएमा वा पूण अंगभागभएमा र.१ लाख २५ हजार,
- काजकैरिया अनुसार योजना : सेवाकलाका सञ्चयकर्ताको मुलु भएमा र.२० हजार,
- सञ्चयकर्तालाई भौगोलिक सहयोग कार्यक्रम, २०७० : साधारण उपचारमा र.२५ हजार र कुछा रोगको उपचारमा र.५ हजार सम्म,
- सुकेसी तथापि रेहायो योजना : महिला सञ्चयकर्तालाई आफ्नो वा सञ्चयकर्तालाई पनी सुकेसी भएमातुकेसी तथापि हुस्तरहाउयोजनालाई तममनेको अधिकतम पटकसम्म प्रति प्रसूतिहु ३२००/-

(घ) अन्य सुविधा:
- कोषको अन्य सुविधा : राहुल लगानी परिवारको परिवारमा सञ्चयकर्तालाई सहभागीता गराइएको (अपर तामाकोशी हाइड्रोपायर विश्वसनको योजनाको सुरक्षा) र अन्य कोषको अन्य सुविधा लगानी परिवारमा प्रस्तुत गरिएको छ।

कोषको प्रतिबन्धाले:
- कोषको दीर्घकालीनविशेष श्रेणीवारू पूर्वाधार विकासको क्षेत्रमाध्यम गरिएको राखिएको आर्थिक विकासको राखिएको तर्कको जोडने, प्रभावकारी स्रोत व्यस्तितां र निन्दितांकार्य सञ्चयकर्ताको माध्यममा सञ्चयकर्तालाई सन्तुलित प्रदान गर्नेछ,
- सुचारू गतिको बत्तिबद्धका आधारमा पुनःश्रृङ्खला सेवाको माध्यममा सञ्चयकर्तालाई सन्तुलित प्रदान गर्नेछ,
- सामाजिक सुरक्षाक्षेत्रको र दायार विस्तारको माध्यममा सामाजिक सुरक्षाको क्षेत्रमाध्यमको पहुँच र योजनामा विकसीय गर्नेछ,
- दशाएँ उच्चविद्यालयविभागीहरूमा सहकार्य र सामूहिकप्रयासको माध्यममा कोषको उत्कृष्ट सामाजिक सुरक्षा संस्थाको संपत्तिकालाई गर्नेछ।

कर्मचारी सञ्चयकोष
पुर्वीको, ललितपुर
Website: www.epfnepal.com.np
IAS/NAS 12 Income Taxes – A Brief Analysis

**History and Background**

In April 2001, International Accounting Standards Board (IASB) adopted IAS 12, Income Taxes which had originally been issued by International Accounting Standards Committee in October 1996. IAS 12 Income Taxes replaced parts of IAS 12 Accounting for Income taxes issued in July 1979. In December 2010, IASB amended IAS 12 to address an issue that arises when entities apply the measurement principle in IAS 12 to temporary differences relating to investment properties that are measured at fair value. That amendment also incorporated some guidance from a related interpretation (SIC 21 Income Taxes – Recovery of Revalued Non depreciable Assets).

The original IAS 12 required an entity to account for deferred tax using either the deferral method or a liability method which is sometimes known as the income statement liability method. IAS 12 (revised) prohibits the deferral method and requires another liability method which is sometimes known as the balance sheet liability method.
In most jurisdiction, accounting profit and taxable profit differ, meaning that the tax charge may bear little relation to profits in a period. Difference arise due to the fact that tax authorities follow rules that differ from NFRS/IFRS rules in arriving at taxable profit. Transactions which are recognized in a particular period, may have their tax effect deferred until a later period. The differences between the two sets of rules will result in different numbers in the financial statements and in the tax computations. The current tax charge for the period will be based on the tax authority’s view of profit, not the accounting view. This means that the relationship between the accounting “profit before tax” and the tax charge will be distorted. The tax charge is the tax rate applied to a tax computation figure and not the accounting figure.

Why Deferred Tax?

Matching concept is significant concept of accounting. According to this concept, income and expense must be recognized in the period to which this relates. IFRS/NFRS rules state that the entity should record its transactions on accrual basis. This means that all the transactions have to be recorded in the period to which it relates. Accounting of the transactions as per NFRS/IFRS and as per taxation rules are different. The charge of tax is based on the profits generated as per taxation laws/rules. To take simple example, Section 19 read with schedule 2 of Income Tax Act, 2058 prescribes the provisions of allowance of depreciation wherein rates of depreciation are stated based on pool of assets. But as per IFRS/NFRS, the depreciation charge is determined based on the useful life of assets. Hence, there is difference of depreciation charge as per tax Laws and IFRS/NFRS rules. This gives rise to deferred tax. Deferred tax could be either in the form of deferred tax liability or deferred tax asset which will be discussed in detail in following paragraphs.

Provisions of IAS/NAS 12

Terminologies

<table>
<thead>
<tr>
<th>Term</th>
<th>Definition</th>
</tr>
</thead>
<tbody>
<tr>
<td>Accounting Profit</td>
<td>is a profit or loss for a period before deducting tax expense</td>
</tr>
<tr>
<td>Tax Profit (Tax Loss)</td>
<td>is the profit (loss) for a period on which income taxes are payable (recoverable).</td>
</tr>
<tr>
<td>Tax Expense (Tax Income)</td>
<td>is the aggregate amount included in the determination of profit or loss for the current and deferred tax.</td>
</tr>
<tr>
<td>Current Tax</td>
<td>is the amount of income taxes payable (recoverable) in respect of taxable profit (loss) for a period.</td>
</tr>
<tr>
<td>Deferred Tax Liabilities (DTL)</td>
<td>are the amount of income taxes payable in future periods in respect of taxable temporary differences.</td>
</tr>
<tr>
<td>Deferred Tax Assets (DTA)</td>
<td>are the amount of income taxes recoverable in future periods in respect of:</td>
</tr>
<tr>
<td></td>
<td>- Deductible temporary differences,</td>
</tr>
<tr>
<td></td>
<td>- Carry forward of unused tax losses,</td>
</tr>
<tr>
<td></td>
<td>- Carry forward of unused tax credits</td>
</tr>
<tr>
<td>Tax base of an asset (liability)</td>
<td>is the amount attributed to an asset (liability) for tax purposes.</td>
</tr>
</tbody>
</table>

Temporary Differences are the differences between the carrying amount of an asset or liability in the statement of financial position and its tax base. As a rule, if the carrying amount of an asset is greater than its tax base the resulting temporary difference gives rise to deferred tax liability. Temporary Difference are of two types;

<table>
<thead>
<tr>
<th>Term</th>
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</tr>
</thead>
<tbody>
<tr>
<td>Taxable Temporary Differences</td>
<td>- which are the debit balances in the financial statements compared to the tax computations and lead to deferred tax credit balances. The detailed examples are cited in examples section.</td>
</tr>
<tr>
<td>Deductible Temporary Differences</td>
<td>- which are the credit balances in the financial statements compared to the tax computations and lead to deferred tax debit balances. The detailed examples are cited in examples section.</td>
</tr>
</tbody>
</table>
Examples of Temporary Differences

A. Examples of circumstances that give rise to taxable temporary differences:

All taxable temporary differences give rise to a deferred tax liability.

Transactions that affect profit or loss
1. Interest revenue is received in arrears and is included in accounting profit on a time apportionment basis but is included in taxable profit on cash basis.
2. Revenue from sale of goods is included in accounting profit when goods are delivered but is included in taxable profit when cash is collected.
3. Depreciation of an asset is accelerated for tax purposes.
4. Development costs have been capitalized and will be amortized to the statement of comprehensive income but were deducted in determining taxable profit in the period in which they were incurred.
5. Prepaid expenses have already been deducted on cash basis in determining the taxable profit of the current or previous periods.

Transactions that affect the statement of financial position
1. Depreciation of an asset is not deductible for tax purposes and no deduction will be available for tax purposes when the asset is sold or scrapped.
2. A borrower records a loan at the proceeds received (which equal the amount due at maturity) less transaction costs. Subsequently the carrying amount of the loan is increased by amortization of the transaction costs to accounting profit. The transaction costs were deducted for tax purposes in the period when the loan was first recognized.
3. A loan payable was measured on initial recognition at the amount of the net proceeds net of transaction costs. The transaction costs are amortized to accounting profit over the life of the loan. Those transaction costs are not deductible in determining the taxable profit of future, current or prior periods.
4. The liability component of a compound financial instrument (for example a convertible bond) is measured at a discount to the amount repayable on maturity. The discount is not deductible in determining taxable profit or loss.

Fair value adjustments and revaluations
1. Financial assets or investment property are carried at fair value which exceeds cost but no equivalent adjustment is made for tax purposes.
2. An entity revalues property, plant and equipment but no equivalent adjustment is made for tax purposes.

B. Examples of circumstances that give rise to deductible temporary differences:

All deductible temporary differences give rise to a deferred tax asset.

Transactions that affect profit or loss
1. Retirement benefit costs are deducted in determining accounting profit as service is rendered by the employee, but are not deducted in determining taxable profit until the entity pays either retirement benefits or contributions to a fund.
2. Accumulated depreciation of an asset in the financial statements is greater than the cumulative depreciation allowed up to the end of the reporting period for tax purposes.
3. The cost of inventories sold before the end of reporting period is deducted in determining accounting profit when goods or services are delivered but is deducted in determining taxable profit when cash is collected.
4. The net realizable value of an item of inventory or the recoverable amount of an item of property, plant or equipment is less than the previous carrying amount and an entity therefore reduces the carrying amount of the asset, but that reduction is ignored for tax purposes until the asset is sold.

5. Research costs (or organization or other start-up costs) are recognized as an expense in determining accounting profit but are not permitted as a reduction in determining taxable profit until a later period.

6. Income is deferred in the statement of financial position but has already been included in taxable profit in current or prior periods.

7. A government grant which is included in the statement of financial position as deferred income will not be taxable in future periods.

Fair value adjustments and revaluations

1. Financial assets or investment property are carried at fair value which is less than cost, but no equivalent adjustment is made for tax purposes.

C. Examples of circumstances where the carrying amount of an asset or liability is equal to its tax base:

1. Accrued expenses have already been deducted in determining an entity’s current tax liability for the current or earlier periods.

2. A loan payable is measured at the amount originally received and this amount is the same as the amount repayable on final maturity of the loan.

3. Accrued expenses will never be deductible for tax purposes.

4. Accrued income will never be taxable.

Recognition of Deferred Tax Liabilities

A deferred tax liability should be recognized for all taxable temporary differences, unless tax liability arises from:

- the initial recognition of goodwill; or
- the initial recognition of an asset or liability in a transaction which:
  - is not a business combination; and
  - at the time of the transaction, affects neither accounting profit nor taxable profit

Recognition of Deferred Tax Assets

- A deferred tax asset should be recognized for all taxable deductible differences to the extent that it is probable that taxable profit will be available against which the deductible temporary difference can be utilized, unless the deferred tax asset arises from the initial recognition of asset or liability in a transaction which:
  - is not a business combination; and
  - at the time of transactions, affects neither accounting profit nor taxable profit

- A deferred tax asset will also be recognized for the carry forward of tax losses and tax credits to the extent that it is probable that future taxable profits will be available against which these losses and credits can be utilized.

- The carrying amount of a deferred tax asset should be reviewed at the end of each reporting period. The carrying amount of a deferred tax asset should be reduced to the extent that it is no longer probable that sufficient taxable profit will be available to utilize the asset.

- Deferred tax asset will be recognized only if the credits or losses can be utilized

Measurement

- The tax rate that should be used is the rate that is expected to apply to the period when the asset is
realized or the liability is settled, based on tax rates that have been enacted by the end of the reporting period. Companies are required to disclose the amount of deferred taxation in the tax expense that relates to change in the tax rates.

- Deferred tax is recognized as an income or expense and included in profit or loss for the period, except to the extent that the tax arises from:
  - a transaction or event which is recognized, in the same or different period, directly in equity or other comprehensive income; or
  - a business combination that is an acquisition.

- Deferred tax should be recognized in profit or loss (i.e. charged or credited to other comprehensive income or directly to equity) if the tax relates to items that are recognized outside profit or loss, in the same or different period.

Business Combinations

Introduction and sources of temporary differences

- Acquisition accounting and equity accounting share certain features in common which are relevant to an understanding of the deferred taxation consequences of employing these techniques.

- Each involves the replacement of cost with a share of net assets and goodwill arising on acquisition, the subsequent impairment of goodwill and the crediting of post-acquisition growth in equity balances to the equivalent equity balances of the group.

- The calculation of goodwill requires a fair value exercise. This exercise may change the carrying amounts of assets and liabilities but not their tax bases. The resulting deferred tax amounts will affect the value of goodwill but IAS/NAS 12 prohibits the recognition of deferred tax arising.

- Deferred tax will be recognized on any fair value differences identified but will not be recognized on actual goodwill figure.

- Retained earnings of subsidiaries (similarly branches, associates and joint arrangements) are included in consolidated retained earnings, but income taxes will be payable if the profits are distributed to the reporting parent.

- Furthermore, IFRS/NFRS 10 Consolidated Financial Statements requires the elimination of unrealized profits/losses resulting from intra-group transactions. This generates temporary differences.

Temporary differences arising on calculation of goodwill

- The cost of acquisition is allocated to the identifiable assets and liabilities acquired by reference to their fair values at the date of exchange transaction.

- Temporary differences arise when the tax bases of assets and liabilities acquired are not affected by the business combination or are affected differently.

- Deferred tax must be recognized in respect of the temporary differences. This will affect the share of net assets and thus the goodwill (one of the identifiable liabilities of the subsidiary is the deferred tax balance)

- The goodwill itself is a temporary difference but IAS/NAS 12 prohibits the recognition of deferred tax on this item.

Intragroup transaction

- IFRS/NFRS 10 requires that unrealized profits and losses arising on inter-company trading must be eliminated on consolidation. Such adjustments may give rise to temporary differences. In many tax jurisdictions it is the individual members of the group that are the taxable entities. As far as the tax authorities are concerned the tax base of an asset purchased from another member of group will be the cost that the buying company has paid for it. Also the selling company will be taxed on the sale of an asset even if it is still within the group. Deferred tax is provided for at the buyer’s tax rate.
Presentation

- Tax asset and tax liabilities should be presented separately from other assets and liabilities in the statement of financial position. Deferred tax asset and liabilities should be distinguished from current tax assets and liabilities.

- An entity should offset deferred tax assets and deferred tax liabilities if, and only if;
  - The entity has a legally enforceable to set off current tax assets against current tax liabilities; and
  - The deferred tax assets and deferred tax liabilities relate to income taxes levied by the same taxation authority on either;
    o The same taxable entity; or
    o Different taxable entity which intent to settle current taxes on net basis

Provisions of Taxation which have potential impact on deferred tax

Provisions in the Income Tax Act, 2058 have special provision with regard to many transactions which create temporary difference and hence they have impact on deferred tax. Few provisions are stated as under.

3. Excess repair, pollution control cost and research & development expenses - As per section 16, 17, 18 of Income Tax Act, there is a limit for allow ability of repair and maintenance, pollution control cost and research and development expenses. Amount in excess of such limit is added to the opening balance of assets for next year for income tax purpose which creates temporary difference.

4. Expenses Provision – Many provisions for expenses are created in financial statements. But as per section 24(2) of Income Tax Act, expenses provision is not allowed for taxation purpose. In this case, tax base of provisions is zero and hence temporary difference is created. For example, expenses for provision for gratuity and leave encashment has been accounted for in the financial statement but may be allowed on payment basis as per Section 24(2) while computing taxable income.

5. Tax Base of Loss – Section 20 of Income Tax Act allows facility of carry forward of losses. It means the losses can be set off against future incomes. Hence temporary difference is created for such losses.

6. Banking business – Section 24(3) of Income Tax Act has accepted the directives issued by Nepal Rastra Bank (NRB) to account for the income and expense. For example as the NRB directives, interest may have been booked on cash basis but in financial statements, it has depreciation charged in both the cases shall be different and accordingly temporary difference arises.

As per schedule 2 of Income Tax Act, assets procured upto Poush end of the income year are capitalized in full, assets procured from Magh to Chaitra are capitalized only 2/3 and assets procured from Baisakh to Ashadh are capitalized by only 1/3. Remaining unabsorbed addition are added for calculation of opening depreciation base for next year. In financial statements every thing procured during the year are capitalized. Due to this temporary difference is created.
to be accounted for on accrual basis. Hence, temporary difference may arise due to interest suspense.

### Examples and Corresponding Accounting Entries

#### Example 1
Attempts have been made to give examples of computation of tax and the accounting entries based on the above provisions for better understanding of the issues.

A company has a profit before depreciation & tax NPR 200,000 in each of five year. Company bought a machinery of NPR 60,000 having useful life of 3 year for accounting purpose but for tax purpose 100% depreciation is allowed in first year. There is also a disallowance of NPR 80,000 in 4th year, out of which NPR 40,000 is allowed in 5th year. Assumed Tax rate for Year 1 & 2 30% and for Year 3, 4 & 5 its 35%. Show the impact on Deferred Tax along with accounting entries.

#### Statement of Profit or Loss

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Year 1</th>
<th>Year 2</th>
<th>Year 3</th>
<th>Year 4</th>
<th>Year 5</th>
</tr>
</thead>
<tbody>
<tr>
<td>Profit before Depreciation and tax</td>
<td>200,000</td>
<td>200,000</td>
<td>200,000</td>
<td>200,000</td>
<td>200,000</td>
</tr>
<tr>
<td>Less: Depreciation</td>
<td>(20,000)</td>
<td>(20,000)</td>
<td>(20,000)</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Accounting Profit (PBT) (A)</td>
<td>180,000</td>
<td>180,000</td>
<td>180,000</td>
<td>200,000</td>
<td>200,000</td>
</tr>
</tbody>
</table>

#### Tax Expense

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Year 1</th>
<th>Year 2</th>
<th>Year 3</th>
<th>Year 4</th>
<th>Year 5</th>
</tr>
</thead>
<tbody>
<tr>
<td>Current Tax</td>
<td>(42,000)</td>
<td>(60,000)</td>
<td>(70,000)</td>
<td>(98,000)</td>
<td>(56,000)</td>
</tr>
<tr>
<td>Deferred Tax</td>
<td>(12,000)</td>
<td>6,000</td>
<td>6,000</td>
<td>28,000</td>
<td>(14,000)</td>
</tr>
<tr>
<td>(B)</td>
<td>(54,000)</td>
<td>(54,000)</td>
<td>(64,000)</td>
<td>(70,000)</td>
<td>(70,000)</td>
</tr>
</tbody>
</table>

#### Profit after tax (A - B)

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Year 1</th>
<th>Year 2</th>
<th>Year 3</th>
<th>Year 4</th>
<th>Year 5</th>
</tr>
</thead>
<tbody>
<tr>
<td>126,000</td>
<td>126,000</td>
<td>116,000</td>
<td>130,000</td>
<td>130,000</td>
<td></td>
</tr>
</tbody>
</table>

#### Computation of Taxable Income

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Year 1</th>
<th>Year 2</th>
<th>Year 3</th>
<th>Year 4</th>
<th>Year 5</th>
</tr>
</thead>
<tbody>
<tr>
<td>Accounting Profit (PBT) (A)</td>
<td>180,000</td>
<td>180,000</td>
<td>180,000</td>
<td>200,000</td>
<td>200,000</td>
</tr>
<tr>
<td>Add: Depreciation as per books</td>
<td>20,000</td>
<td>20,000</td>
<td>20,000</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Less: Depreciation as per Income Tax</td>
<td>(60,000)</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Add: Disallowance</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>80,000</td>
<td>-</td>
</tr>
<tr>
<td>Less: Allowance</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>(40,000)</td>
<td>-</td>
</tr>
<tr>
<td>Taxable Profit</td>
<td>140,000</td>
<td>200,000</td>
<td>200,000</td>
<td>280,000</td>
<td>160,000</td>
</tr>
<tr>
<td>Tax Rate</td>
<td>30%</td>
<td>30%</td>
<td>35%</td>
<td>35%</td>
<td>35%</td>
</tr>
<tr>
<td>Current Tax</td>
<td>42,000</td>
<td>60,000</td>
<td>70,000</td>
<td>98,000</td>
<td>56,000</td>
</tr>
</tbody>
</table>

#### Deferred Tax Computation

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Year 1</th>
<th>Year 2</th>
<th>Year 3</th>
<th>Year 4</th>
<th>Year 5</th>
</tr>
</thead>
<tbody>
<tr>
<td>Opening balance of timing difference</td>
<td>-</td>
<td>(40,000)</td>
<td>(20,000)</td>
<td>-</td>
<td>80,000</td>
</tr>
<tr>
<td>Addition</td>
<td>(40,000)</td>
<td>-</td>
<td>-</td>
<td>80,000</td>
<td>-</td>
</tr>
<tr>
<td>Deletion</td>
<td>-</td>
<td>20,000</td>
<td>20,000</td>
<td>-</td>
<td>(40,000)</td>
</tr>
<tr>
<td>Closing balance</td>
<td>(40,000)</td>
<td>(20,000)</td>
<td>-</td>
<td>80,000</td>
<td>40,000</td>
</tr>
<tr>
<td>Tax Rate</td>
<td>30%</td>
<td>30%</td>
<td>35%</td>
<td>35%</td>
<td>35%</td>
</tr>
<tr>
<td>Deferred Tax</td>
<td>(12,000)</td>
<td>(6,000)</td>
<td>-</td>
<td>28,000</td>
<td>14,000</td>
</tr>
<tr>
<td>DTA/DTL to be shown in Balance sheet</td>
<td>DTL</td>
<td>DTL</td>
<td>NIL</td>
<td>DTA</td>
<td>DTA</td>
</tr>
<tr>
<td>Amount for Profit or Loss</td>
<td>(12,000)</td>
<td>6,000</td>
<td>6,000</td>
<td>28,000</td>
<td>(14,000)</td>
</tr>
<tr>
<td>To be debited/credited to Profit or Loss</td>
<td>Debited</td>
<td>Credited</td>
<td>Credited</td>
<td>Credited</td>
<td>Debited</td>
</tr>
<tr>
<td>Reason for Debit/Credit</td>
<td>Creation of DTL</td>
<td>Reversal of DTL</td>
<td>Reversal of DTL</td>
<td>Creation of DTA</td>
<td>Creation of DTA</td>
</tr>
</tbody>
</table>

#### Accounting Entries

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Year 1</th>
<th>Year 2 &amp; 3</th>
<th>Year 4</th>
<th>Year 5</th>
</tr>
</thead>
<tbody>
<tr>
<td>Profit or Loss A/C Dr</td>
<td>12,000</td>
<td>DTL A/C</td>
<td>12,000</td>
<td>6,000</td>
</tr>
<tr>
<td>To DTL A/C</td>
<td></td>
<td>To Profit or Loss</td>
<td>6,000</td>
<td></td>
</tr>
</tbody>
</table>

#### Example 2

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Year 1</th>
<th>Year 2 &amp; 3</th>
</tr>
</thead>
<tbody>
<tr>
<td>Non-Current Assets</td>
<td>460,000</td>
<td>320,000</td>
</tr>
<tr>
<td>Accrued Interest</td>
<td>18,000</td>
<td>-</td>
</tr>
<tr>
<td>Receivable</td>
<td>(15,000)</td>
<td>-</td>
</tr>
<tr>
<td>Payable</td>
<td>-</td>
<td>-</td>
</tr>
</tbody>
</table>

The balance on deferred tax balance account on July 16, 2014 was NPR 10,000. This was calculated at a tax rate of 30%. During 2016 the government announced an unexpected increase in the level of corporate income tax up to 35%. Set out the movement on deferred tax account.

#### Solution

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Deferred Tax NPR</th>
</tr>
</thead>
<tbody>
<tr>
<td>Deferred Tax as at July 16, 2014</td>
<td>10,000</td>
</tr>
<tr>
<td>Profit or loss – change in tax rate</td>
<td>1,167</td>
</tr>
<tr>
<td>Opening balance restated (10,000*35/30)</td>
<td>11,167</td>
</tr>
<tr>
<td>Profit or loss – origination of temporary differences</td>
<td>38,383</td>
</tr>
<tr>
<td>Deferred Tax as at July 15, 2015 (see working)</td>
<td>50,050</td>
</tr>
</tbody>
</table>
Working

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Carrying Amount NPR</th>
<th>Tax Base NPR</th>
<th>Temporary Difference NPR</th>
</tr>
</thead>
<tbody>
<tr>
<td>Non-Current Assets</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Accrued Interest</td>
<td>460,000</td>
<td>320,000</td>
<td>140,000</td>
</tr>
<tr>
<td>Receivable</td>
<td>18,000</td>
<td>-</td>
<td>18,000</td>
</tr>
<tr>
<td>Payable</td>
<td>15,000</td>
<td>-</td>
<td>(15,000)</td>
</tr>
<tr>
<td>Deferred Tax Liability (DTL)</td>
<td></td>
<td>55,300</td>
<td></td>
</tr>
<tr>
<td>Deferred Tax Assets (DTA)</td>
<td></td>
<td>(5,250)</td>
<td></td>
</tr>
<tr>
<td>Deferred tax (DTL) – net</td>
<td></td>
<td>50,050</td>
<td></td>
</tr>
</tbody>
</table>

Summary of IAS/NAS 12

It is recommended to follow the steps given below while calculating deferred tax under IAS/NAS 12.

- Set out the carrying amount of every asset and liability.
- Calculate the tax base for each asset and liability.
- Calculate the temporary difference by deducting the tax base from the carrying amount using the following proforma:
  Asset/Liability  Carrying Amount  Tax Base  Temporary Difference
- Calculate the deferred tax liability and asset.
- Calculate the net deferred tax liability or asset by summing the deferred tax liability and deferred tax asset.
- This will be the asset or liability carried in the statement of financial position. If it is not appropriate to offset the asset and liability they should be shown separately.
- Calculate any amount to be recognized outside of profit or loss – by multiplying the amount taken to the comprehensive income or directly to equity by the rate.
- Deduct the opening deferred tax liability or asset to give the profit or loss charge/credit.
- Where there has been a change in the tax rate it is necessary to calculate the effect of this change on the opening deferred tax provision. Follow the same procedure mentioned above, calculating the required closing deferred tax liability or asset and the charge/credit to profit or loss.

- The charge/credit to profit or loss is then analyzed into the amount that relates to the change in the tax rate and the amount that relates to the temporary differences.
- The amount that relates to the change in tax rate will equal the amount of the temporary difference in the previous period $\times$ the change in the tax rate.

Conclusion

In essence, Deferred Tax is neither deferred nor a liability. It is simply the impact of difference between the accounting treatment and tax treatment of a particular transaction. There may be certain rules mentioned in tax laws (in Nepalese context Income Tax Act, 2058) of a particular country which may be different from the rules mentioned in respective country’s generally accepted accounting principles (in Nepalese context NAS/NFRS). Though deferred tax is mandatorily required to be accounted for in the books of account, it is worth to note the following points while recognizing it.

1. Liability to be recognized in full (subject to certain specific exemptions) but assets should be recognized to the extent it is probable that taxable profit will be available against which deductible temporary difference can be utilized. This is an application of the concept of ‘prudence’.

2. Deferred tax and the framework

As we have seen, IAS 12 considers deferred tax by taking a balance sheet approach to the accounting problem by considering temporary differences in terms of the difference between the carrying values and the tax values of assets and liabilities – also known as the valuation approach. This can be said to be consistent with the IASB Framework’s approach to...
recognition within financial statements. However, the valuation approach is applied regardless of whether the resulting deferred tax will meet the definition of an asset or liability in its own right.

Thus, IAS 12 considers the overriding accounting issue behind deferred tax to be the application of matching – ensuring that the tax consequences of an item reported within the financial statements are reported in the same accounting period as the item itself.

For example, in the case of a revaluation surplus, since the gain has been recognized in the financial statements, the tax consequences of this gain should also be recognized – that is to say, a tax charge. In order to recognize a tax charge, it is necessary to complete the double entry by also recording a corresponding deferred tax liability.

However, part of the Framework’s definition of a liability is that there is a ‘present obligation’. Therefore, the deferred tax liability arising on the revaluation gain should represent the current obligation to pay tax in the future when the asset is sold. However, since there is no present obligation to sell the asset, there is no present obligation to pay the tax.

Therefore, it is also acknowledged that IAS 12 is inconsistent with the Framework to the extent that a deferred tax asset or liability does not necessarily meet the definition of an asset or liability.

3. Deferred tax assets and liabilities represent future taxes that will be recovered or that will be payable. It may therefore be expected that they should be discounted to reflect the time value of money, which would be consistent with the way in which other liabilities are measured. IAS 12, however, does not permit or allow the discounting of deferred tax assets or liabilities on practical grounds.

References:
1. www.ifrs.org
2. Income Tax Act, 2058
3. Deferred Income Taxes – Principles and Examples by CA Bhava Nath Dahal
4. Various webpages
TAXATION

Considerations for Tax Audit

Background

Audit means examination of books of account for the purpose of providing opinion on true and fairness of fact and records. Audits are of different types, but most commonly used term in private sectors are statutory audit and tax audit. Statutory audit is made mandatory by law namely Company Act, Income Tax Act, specific acts etc. It is conducted independently by the professionals to verify the financial statements with accounting records. The purpose of statutory audit is to ensure credibility, transparency and accountability of financial statement. The statutory auditor expresses opinion on true and fairness of final accounts as well as compliance with relevant laws. However, tax audit has two fold. It is defined as an audit of the accounts of the taxpayer, by a professional auditor to fulfill the requirement of Income Tax Act while filling tax return. The examination of tax return by the tax authority to verify the accurateness of income and deductions is also called tax audit. However, this article focuses on the tax audit conducted by professional auditor.

The main focus of the tax auditor has to ensure compliance with statutory provisions regarding computation, calculation, application of correct tax rates, assessment procedure etc. by the taxpayers while determining the tax liability. Similarly, the obligation of tax auditor as an advisor of the tax payer is to certify and submit the following documents with tax return.

Mr. Ramu Prasad Dotel
Mr. Dotel is a Assistant Auditor General of OAG/N. He can be reached at ramu_dotel@hotmail.com
Obligation of the Tax Auditor

As per Income Tax Act, 2058 and Directives issued by Inland Revenue Department (IRD), the auditor should certified balance sheet, income and expenditure account, cash flow and tax return of the tax payer whose turnover is more than Rs. 10 million from fiscal year 2073/74. It is mentioned in the Directives that the person who certifies the tax return is the tax auditor. Such auditor should be responsible to certify that accounts and records are kept in line with tax law and represent true and fair view of income, expenditure, profit, loss, assets and liability of the tax payer. They should ensure that all formats, checklists, documents and statements required by law have been submitted with tax return. The role of tax auditor as specified in Income Tax Act and Directive is to assure right taxation, whether the audit is carried out by professional auditor.

Currently, Nepal has adopted self-assessment system of tax administration. This system has entrusted crucial responsibility to the professional tax auditor. Therefore, the tax auditors have become an integral part of the tax system working as intermediaries assisting taxpayers to deal with their tax matters.

These auditors can promote the good governance by assessing right taxation on behalf of their client. However, the sole responsibility of submitting tax return remains to the tax payer and tax auditors who are professional responsible to provide tax advice or assess tax liability of the tax payer. The Income Tax Act also states that professional accountant if they provide suggestion or assess tax, which is not in spirit of tax laws that may cause revenue leakage. Such activity must be taken as financial crime. Thus, government has recently introduced provision of penalizing auditor, if they support in evading tax by providing and certifying false documents knowingly. It is also a matter of ethical issue and professional auditors are required to comply with the Code of Ethics issued by Institute of Chartered Accountant of Nepal (ICAN).

It may be argued that fair presentation is the responsibility of tax payer and tax payer obliged to present actual income and expenditure of their business. If tax payers fail to comply with such requirement, penalty might be enforced on them. It is unfair to penalize the tax auditor. However, it is special purpose engagement for auditor required by law to fulfill the obligation of the regulator. Nepal Standards on Auditing also suggests about discharging legislative requirement. In this context, the professional auditors need to consider acceptance and continuance of such engagement considering the ethical requirement, competence, independence and their limitation.

The main focus of the tax auditor has to ensure compliance with statutory provisions regarding computation, calculation, application of correct tax rates, assessment procedure etc. by the taxpayers while determining the tax liability. Similarly, the obligation of tax auditor as an advisor of the tax payer is to certify and submit the following documents with tax return. In addition, if they are not satisfied with the documents submitted or materially misstated, as per Income Tax Act, they should certify by qualifying their dissatisfaction. Some of the key documents that need to be submitted with the tax returns are stated below:

- Financial statements- Balance Sheet, Profit and Loss Account, Cash Flow Statement and other related annexure,
- Statements of purchase, sales, debtor, creditor over than 100 thousand rupee,
- Tax assessment and tax adjustment forms,
- Statements of tax deduction and deposit,
- Amount deposited to retirement fund on behalf of their staff,
- Date-wise assets purchased, disposed statements,
- Calculation of category-wise depreciation base of assets, yearly depreciation and repair and maintenance expenditure,
- Statement of allowable and capitalized interest, research and development expenditure,
➢ Tax deducted at source and deposited,
➢ In case of stock, opening and closing stock with quantity and value indicating valuation,
➢ Calculation of cost of goods sold,
➢ Insurance expenses and claim received during the year,
➢ Statement of receivable, payable written off,
➢ Contingent liability and change in capital structure,
➢ Justification of income or expenditure included in income and expenditure account but not in income return,
➢ Non-taxable income and related expenditure,
➢ Exchange gain loss statement,
➢ Detail of import/export including payment through letter of credit,
➢ In case of industry, details of finished product and by-product and their cost, raw materials, packing materials, import, local purchase, production, sales, stock of raw materials and finished product, wastage, recovery rate, selling price and valuation of closing stock,
➢ In case of contractor, contract agreement, cost estimate, contract wise income and expenditure, price variation, work addition deletion, payment certification letter,
➢ In case of commission based taxpayer, contract agreement and term of payment, commission rate,

It is worth to note that in course of detail audit of tax returns by Internal Revenue Offices, if the Tax Officers is not satisfied that the returns filed by taxpayers are incomplete, incorrect, etc. then the officer may raise questions and assess additional tax. So the taxpayers and tax consultants need to be very careful in submitting the tax returns.

Considerations for Tax Audit

Generally, taxpayers submit their tax return with the help of professional auditors. Presently, there are more than 1.2 million taxpayers and professional auditors review all tax returns of those which has turnover more than 10 million. However, tax authority carry out tax audit of less than 2 percent tax returns filed considering the risk factor and volume of transaction. It is apparent that Nepalese tax system completely rely on professional accountant.

At present, tax authority assesses substantial amount of additional tax liability to each and every selected tax payer on the ground of true and fairness of statements. Thus, tax related risk in audit profession is increasing day by day in developing countries like Nepal. In the view of this situation, the Professional accountant rendering tax consultancy are required to consider several risk factors, which are given below as some examples.

<table>
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<tr>
<th>S. No</th>
<th>Heading</th>
<th>Details</th>
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<tbody>
<tr>
<td>1</td>
<td>Presentation of Financial Statements</td>
<td>Many statements submitted along with tax return are incomplete and contradict each other. Disclosure is crucial statement related to account of tax payer. However, professional accountants do not submit complete disclosure as per accounting standards, tax laws and directives. Many tax auditor sign the balance sheet and profit and loss account which do not give previous year’s figures and even the account heading are not consistent as per standard. Some of them do not even mention method of stock valuation. In this situation, tax authority may interpret the account differently and assess tax liability.</td>
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<tr>
<td>2</td>
<td>Non Submission of Documents</td>
<td>Non-submission of all required documents as specified in the tax laws and directives. Many of the tax payers do not submit the statements of purchase, sales, debtor and creditor valued over than Rs. 100 thousand, which create mismatched transaction. Likewise, many of them do not submit documents as per their specific nature of transaction. It may create misunderstanding between tax authority and tax payer which may result in additional tax liability.</td>
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</tbody>
</table>
Industry consumes raw materials to produce finished goods. Ratio of raw material consumption play vital role in determining profit as well as tax liability. Ministry of Industry has determined recovery rate of the raw material for liquor, steel, cement, noodles and other products. IRD has endorsed the same recovery rate for tax purpose. Non-compliance to the recovery rate determined by Ministry of Industry is another risk area for tax audit.

- Capital gain on selling of tax payer's business is another area for tax evasion. Likewise, revaluation of assets and liability and submitting separate return, in case of ownership change is the key area to ponder in tax audit.
- Foreign contractor that have signed agreement for carrying out construction works or supply of goods in Nepal either needs to submit income tax return as a permanent establishment including all income received in Nepal and payment made to the contractor directly to their home country or paid 5 percent TDS in foreign portion payment as a non-residence. However, this provision has not been complied with. This is another risk area of revenue leakage.

### 3. Documents Mismatch

- Purchase and sales figures submitted in return details for purpose of value added tax (VAT) and income tax return are not reconciled. Likewise, purchase and sales submitted in monthly return details does not match with the yearly income tax return. In this regards, verification and reconciliation are the crucial obligation of tax auditor. It is worth to note that mismatch of transaction could lead to leakage of revenue.
- Comparison of outstanding tax liability and tax adjustment claimed in different year are not matched. If justification is not provided, account may be interpreted differently.
- Sales shown in the return detail and tax deducted at source (TDS) claimed should be matched. If any discrepancy occurs need to be justified.

### 4. Non Compliance with Legislations

- Loans taken for business purpose may be used for providing advance and loan to the director or diverted to other sister concern without any return or less return. Such practice is against the provision of Banking Offence and Punishment Act, 2008. It may reduce the tax liability and ultimately helps to revenue leakage. The tax auditor should be cautious on such events.
- According to VAT Act, 2052 and VAT Rule, 2053, while carrying out both the taxable and non-taxable business, the VAT should be credited in proportional basis. Likewise, only the amount of tax paid on purchases related to business can be offset. In some cases, sales are exempted, however, purchase are not exempted. Tax payer may claim full credit on purchases as a result of which ineligible VAT credit and revenue leakage. Tax auditor need to focus on such matter.
- Income Tax Act provides different tax rates and rebate according to nature and types of business. However, applicable tax rate and allowing rebate is another area of mistake.
- As per Bonus Act, seventy percent of the residual amount after distribution from the allocated amount for bonus needs to be deposited to the Enterprise Level Welfare Fund and remaining thirty percent to the National Level Welfare Fund, established by Government of Nepal. While depositing amount in the Enterprise Level Welfare Fund, tax shall be deducted on source at the highest rate applied in income of natural person. Likewise, undistributed provision of bonus should be disallowed for tax purpose. The allocation, distribution and deposit of bonus are the areas of concern to tax auditor.
TAXATION

• Income Tax Act states organization established without having a profit motive which carries out transactions according to its objectives shall be entitled to tax exemption, while tax exemption cannot be allowed if such organization carried any other business. Tax auditor should be careful regarding business conducted by the getting tax exempted certificate.

• Interest paid on loan by the employee during the year is lower than the interest to be paid as per the prevailing standard interest rate, the amount to the extent it is lower shall be characterized and included in taxable income of the employee. Different bank, financial institution and corporate bodies are providing loan on concessional basis. However, the difference in interest rate has not been characterized.

• While constructing the building, apartment and other infrastructure works by the taxpayer, it should be done through VAT registered firm. If any purchase made from non-registered firm, the respective VAT amount needs to be paid by the taxpayer. Tax auditors are required to consider this provision of VAT Act.

5. Related Party Transaction

• Related party transaction should be disclosed and identified whether such transactions are in arm length principle or not. However, this practice is not satisfactory. Many tax auditors either do not disclose or investigate related party transactions, which may have material impact in tax liability.

6. Ratio Analysis

• The tax auditors giving due respect to the account of the tax payer, need to scrutinize and analyze different ratios such as: energy (fuel and electricity) consumption and production, wages and production, debtor turnover, gross profit, net profit ratio etc.

Conclusion

In case of tax audit, the Standards on Auditing suggest that, professionals who are engaged for audit of special purpose financial statements which are prepared in accordance with a financial reporting framework designed to meet the financial information needs of specific users. Those financial reporting provisions are established by regulator that need to be fulfilled by the taxpayers as regulatory requirements specified by Regulation. Practically, IRD is the regulator which has prescribed the required documents to be submitted along with tax return is the special purpose financial statements or requirements. The auditor needs to fulfill requirement of relevant legislation in case of special purpose engagement.

Normally, many tax auditors are unaware of such legal requirement. Thus, non-compliance of tax provision is wide spread in Nepal and government is bound to introduce mechanism of penalizing the tax auditor. The significance of tax auditor under self-assessment tax system has increased due to reasons that include rapid expansion of the scope and complexity of tax law, growth in complexity of business operations of economy, increased investment activities of individual taxpayers etc. In this context, the tax auditor should be more responsible in certifying tax return. However, there are several common risk factors relating to not submitting required true and fair documents, submission of incomplete documents, reconciliation of figures relating to different statements, making disclosure, compliance to the provision of tax laws described in earlier section of this article, which required special attention on behalf of professional auditor.

References
1. 53rd Audit Report, 2072, Office of the Auditor General, Babarmahal, Kathmandu
2. Income Tax Act, 2058 and related Rules
3. Value Added Tax Act, 2053 and related Rules
4. Income Tax Manual, 2068, Inland Revenue Department, Lazimpat, Kathmandu
5. Nepal Standard on Auditing 800, Auditing Standards Board, Nepal
Income tax is levied in the income of a person. If there is no income tax in that income, return to the investor will be higher. For example, if Rs.1000 of investments earn Rs.100 in a year before income tax of 25%; profit before tax is Rs.100 (10% of investment), income tax is Rs.25 (25% of income) and ultimate return to the investor is Rs.75 (7.5% of investment). This is why, income tax is major cost for the return to the investor (tax to net-return ratio is 1:3 in above example). Taking the dividend tax or repatriation tax, actual return will be lower than above too.

Considering income tax is one of the major cost for the return to the investors, States allow the tax concession to attract huge amount of investments- especially for the infrastructure and industrial investments. Tax concessions, in contrast, cannot attract the foreign investments even there is full exemption to foreign investors.

We have not analyzed the impact of taxation in foreign investment. ‘How much direct investment will flow into Nepal, if it allows full tax exemption’ has a readymade answer of enough or more than we desire. The reality in substance is different than this.
There are more than twenty factors that affect the foreign investment in any country, directly or indirectly. Taxation is one average factor out of them, but not major amongst them. The reason is, excluding very few example, investor has tax obligation. Tax exemption in source or tax concession in source, normally, do not reduce their ultimate tax burden.

In the existing Nepal’s tax regime, there are many instances of tax concession and many of them are designed to attract foreign direct investments. Investments in the sector of manufacturing industries (except negative externalities), hydro-electricity or alternative electricity, tourism, information technology, petroleum extraction etc. are designed to attract huge amount of foreign investments.

Let’s discuss the impact with real case of tax concession in Nepal tax. There is full tax concession for the first 10 years from the date of generation of electricity, if this date falls upto 2080 Chaitra-end. Only 50% of applicable tax is levied for next 5-years. Concession in tax would be, of course, high rate of return with early pay-back. Assuming local tax rate of foreign investor is 30% in their own country. In the tax view point, this policy has four deficiencies.

Firstly, the investor will not receive any tax benefit, even Nepal allows full tax concession. In case the Hydel Company earns, say, Rs.1000 Crores. Based on tax concession, no tax is levied here and profit after tax is Rs.1000 Crores. But, investor is foreigner, and will have to pay domestic tax at 30% on their own country, resulting ‘effective profit after tax’ to the investor is equivalent to Rs.700 Crores. How much would be after tax profit, if Nepal tax rate is 20% in Hydel? This would be Rs.200 Crores in Nepal and equivalent of Rs.100 Crores in their own country and ultimately after tax income would be Rs.700 Crores. Levy tax in Nepal or concession has not affected it’s after tax income. In fact, tax concession to foreign investor, except few exception as below, is meaning-less concession. It shifts the tax from Nepal treasury to foreign country treasury.

Secondly, equity portion in any Hydel project is a small proportion comparing to debt financing and spontaneous financing. There is no tax concession for the return to the debt (interest, commission or other charges). Nepal tax do not recognize the spontaneous financing as a source of financing and may have even tax administration burden to the investor. Had tax would be an attraction, the exact benefit is allowed to a part of gross investment which employed as equity.

Thirdly, there are few extra-ordinary anti-avoidance measure employed in earlier year of business. Depreciation is one major example. There is compulsory depreciation including compulsory acceleration for tax in the beginning of the business. Major portion of capital investment base will compulsorily depreciate during the period of tax concession. After concession period, there would be unattractive depreciation base causes the high tax. In the manufacturing or infrastructure business, method for repair allowance is demotivating rewards for investors. We know the new machine or installation requires low repair cost and old equipment or installation requires high repair cost. Sometimes, repair cost in old equipment or machinery would be so high (beyond economic repair, BER), to the owner and motivates to replace it. There is high limit of repair in the new equipment and this limit falls when it becomes old. Again after concessional period, real repair cost will be disallowed, results high tax.

Above cases are similar for any type of tax concession which were intended for foreign investments like manufacturing, infrastructure, service-sector, information technology, tourism or other. Attracting foreign investor, tax concession is not a good tool. Minor activity of central bank, for example, would be very influencing factor to the foreign investor than periodic tax concession or no tax forever.
Fourthly, foreign investors have expertise of investment in the country having vulnerable public administration including tax administration. No foreign investors relies the tax administration, where the country adopts withholding tax practices in normal business transactions (except for employment). Withholding tax procedures always creates ambiguities and judge is always the taxation authority who are complaints also. Internationally, tax concession is strictly interpreted in favor of taxation authority. To obtain the concession, each and every provision of tax conditions must be fulfilled by tax payer. In case, assessing officer rejects the tax concession showing minor deviations, there would no remedy to the taxpayer/investor. There would be appeal mechanism; however, ultimately assessing officer is judge there. Eventually such practices demotivate experienced foreign investor in the tax matters.

Withholding tax on normal business transaction will create the ambiguity for tax obligation. For example, purchase of equipment from foreign country, there is income of exporter in own country and tax on importing country will not levied to the exporter. But, country employing withholding tax on normal business transaction seeks withholding tax in import. Taking example of Nepal, non-resident do not require to pay tax if they have not business income in Nepal as per Nepal tax law. In case a Hydel Company imports electro-mechanical equipment, 5% withholding tax requires to withheld as per another Section of tax law. Exporting party, of course, do not pay the Nepal tax as per international practice or showing Nepal tax law. But, importing party obliges for withheld the tax; this means 5% of import cost will be paid by the Hydel Company as gross-up procedure. The tax concession during business period has paid in advance during constructor period here. Similar cases will be occurred for interest during construction too. Foreign investor will recover interest delay with grace-period during construction because of reason of cash-flow to the developer. Tax on that interest will be levied at the point of accounting of interest during construction. Here, debt-financer realizes the short-fall of cash-flow during construction, but taxation authority having tax concession facility fails to realize same. In most of the case of withholding tax procedure, this will either be grossed up burden to the developer or early financing requires to them.

Then, question may arise, why tax-heaven are attractive to the foreign investors or black-money owner? The reason is not the tax or tax-heaven, but the loose corporate environment and tight information policy. If an investor registers a company in Nepal, practically winding up is extremely difficult; if a labor works for 240 days, many practical difficulties requires to remove him/her; if a company earns profit and wants to repatriate dividend, transferring bank seeks tax-paid -certificate during tax concession period etc. are more decisive factor for foreign investor than tax concession. In the tax-heaven countries they have- most easy process for registering a company or liquidation - within one or few days; no-labor restrictions, easy and fast administrative procedure, fast judicial process; restriction-less money transfer/wire-transfer etc.

Tax concession to the foreign investor may be sometimes beneficial to the real investor in case there is double tax avoidance agreement either with exemption method of elimination of double tax or with tax sparing provision.

In the exemption method of elimination of double taxation, domestic investor having foreign income is exempt for local tax; so, tax benefits from the Source-State fall in the pocket of investor.

In the credit method of elimination of double taxation, tax sparing method within the credit method will bring-back the tax concession to the pocket of investor. In tax sparing method, resident country levies the tax in foreign source income assuming, the deemed payment of tax to the extent of concession allowed in the source country.
Nepal has entered into tax treaties with 10 States-Austria, China, India, Korea, Mauritius, Norway, Pakistan, Qatar, Sri Lanka and Thailand. There is good condition of Tax Sparring Provision in all those ten tax treaties, except obstacles with Austria and Norway. Under Tax Sparring Provision, the tax concession in the source country deemed to be as tax paid for the purpose of tax calculation in resident country of the investors. For example, if a Chinese investor invests equity capital in hydro-electricity project in Nepal, there is tax concession for first 10 years. In the absence of tax concession, there is tax of 20% of profit. Chinese investors receive full income due to tax concession, and Chinese taxation authority allows Nepal tax credit of 20% based on Tax Sparring Provision under Para 3 of Article 23 of tax treaty of Nepal and China. Similar benefit will receive by the investors from other treaty-countries except investors from Austria and Norway.

In the case of investors from Austria, there is Tax Sparring Provision in the tax treaty, but Austria exempts Nepal income for Austrian tax as exempt method of double taxation, but it uses exemption with progression. Due to exemption method, out tax concession is benefit to the Austrian investors in Nepal. But exemption with progression of Austrian tax, it increases the tax burden to the investors and intended benefit will be lower than Nepal allows as concession.

In the case of investors from Norway, there was Tax Sparring Provision for the first 10 years which lapsed the benefit period now. Any tax concession from Nepal tax to the Norwegian investors in Nepal, now obtains tax concession here, but requires to pay whole tax in Norway. This will shift the tax concession from Nepal treasury to the Norwegian treasury.

Apart from above cases, all the foreign equity investors will not obtain any tax benefit from concession in Nepal. In all cases, debt-investors will not obtain any tax concession.

Some of the tax concessions are for public-consumption only. For example, we can discuss the tax concession in information technology. Nepal tax law allows few tax concessions in specified IT-business having operated in specified places of business-parks. Unfortunately, we have no such technical parks, where any tax concession may be waived for the information business-holder. Second example is establishment of manufacturing industry in the Special Economic Zone (SEZ). We planned to establish SEZ since last 30 years, but have none. Third example would be tax concession on sale of or export of intellectual property, where its registration law is extremely weak to obtain own right.

What can we do for attracting foreign investments? Even income tax is one of the major cost for the return to the investor, this is not major factor for investing in any project or in any country. Person having income pays tax, if and only if there is good business environment. For taxation, minor harassment may demotivate the investor. We should concentrate to resolve those minor tax factors which may cause the investor heavy administrative burden. Repatriation of income is another crucial factor for investors. Consider, there is tax concession and banker, as instructed by a circular of tax administration, does not allow the repatriation of income without tax paid documents. This is minor administrative burden, but all the investing environment has collapsed easily.
Tax Exemptions and Concessions: An Overview

1. Background

The new Income Tax Act has repealed the provisions regarding Income Tax in the various Acts. The aim of providing such benefits are numerous such as promoting a backward or prioritized sector or industry, removing regional disparity by encouraging industry to set up in a particular region or sector, reducing unemployment problem or making the optimal use of local resources.

![Diagram showing the flow of concessions and benefits]

2. Basis of Concession

BASIS OF CONCESSION

STATUS OF PERSON

.getEntityType

BUSINESS TYPE

SPECIAL INDUSTRY
AGRICULTURAL INDUSTRY
TOURISM INDUSTRY
INFORMATION TECHNOLOGY INDUSTRY

TRANSACTION

Providing

Complete relief from taxes
Reduced rates
Tax on only a portion of income

3. Business Exemption and Concessions

Business exemptions and concession means the benefits, facilities and rebate to a particular industry or sector. These benefits may be in the form of tax holiday or lower tax rate. Before the enactment of Income Tax Act, 2058, other Acts, like Industrial Enterprises Act, Pension Fund Act, etc had provisions to
allow tax exemption and tax concession. But the new Income Tax Act has repealed the provisions regarding Income Tax in the various Acts. The aim of providing such benefits are numerous such as promoting a backward or prioritized sector or industry, removing regional disparity by encouraging industry to set up in a particular region or sector, reducing unemployment problem or making the optimal use of local resources.

Business concession and exemptions are offered by Section 11 of Income Tax Act, 2058 in either of the following way:

❖ **By way of exemption:**

Exempted income such as agricultural income of a farmer, rural based cooperatives shall not be required to be included in income tax returns. In other words, for tax purpose such income shall not be treated as taxable income. Person earning exempted income only shall not be required to file income tax return.

❖ **By way of deducting from assessable income:**

In some cases concession is allowed after including in income from business/investment, but deducting from assessable income such as Special Economic Zone (Hilly), Special Economic Zone (Other), Remote Industry, Information Technology Industry.

❖ **By way of tax credit or reduced rate:**

In such cases income shall be included in tax returns and proportionate or other credit is allowed on tax amount or reduced rate of tax shall be applied on taxable income. In other words, the income shall be deemed as normal income but concession shall be provided on tax amount.

<table>
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<tr>
<th>Section</th>
<th>Heading</th>
<th>Conditions to be satisfied</th>
<th>Treatment</th>
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</table>
| 11(1)   | Income from Agriculture | An agricultural income:  
  ➢ Derived from sources in Nepal  
  ➢ Not by a registered firm, or company, or partnership, or a corporate body  
  ➢ Not through the land above the holding ceiling as prescribed in the Land Act, 2021. | Fully Exempt  
(Please refer Example 4(i) Below) |
| 11(2)   | Income Derived by Certain Cooperative Societies | i. Incomes derived by cooperative societies from:  
  ➢ agriculture and forest products  
  ➢ Forestry related business  
  ➢ Agricultural tools (other than machine operated) and  
  ➢ Income of Rural community based saving & credit cooperatives.  
  ii. Income of Rural community based saving & credit cooperatives. | Fully Exempt. (Please refer Example 4(ii) Below)  
Dividends distributed by such societies are also exempt from tax. |
| 11(3)(Ka) | Concessions available to Special Industries and Information Technology Industries having certain number of employees | Income derived from sources in Nepal  
  ➢ From a special industry providing direct employment to Nepalese Citizen for the whole year:  
  • To 300 or more.  
  • To 1200 or more  
  • To more than 100 including at least 33% women, appressed or handicapped.  
  and  
  ➢ Information technology industry providing direct employment to Nepalese Citizen for the whole year:  
  • To 300 or more | Shall be taxable at:  
(Please refer Example 4(iii) Below)  
• 90% of the applicable tax  
• 80% of the applicable tax  
• 80% of the applicable tax for special industry providing direct employment for the whole year  
• 90% of the applicable tax |
<table>
<thead>
<tr>
<th>11(3) (Ka1)</th>
<th>Concession to certain Industry, having certain employment</th>
<th>Providing direct employment to 100 Nepalese Citizens shall be taxed at 70% of Normal rate.</th>
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<tr>
<td></td>
<td>i. Special industry</td>
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<td>ii. Agro-based industry or</td>
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<td></td>
<td>iii. Industry related with tourism sector</td>
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<td>11(3) (Kha)</td>
<td>Concession to Special Industries established in various areas</td>
<td>Special industry run in</td>
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<td>Very undeveloped areas</td>
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<td>Undeveloped and</td>
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<td>Underdeveloped areas</td>
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<td>Shall be taxable at:</td>
<td>10 %</td>
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<td>20 %</td>
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<td>30 %</td>
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<td>Of the applicable tax for 10 income years including the income year in which such industry is commenced.</td>
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<td>(Please refer Example 4(iv) Below)</td>
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<tr>
<td>11(3) (Ga)</td>
<td>Concession to Special Industry certain investment and employees</td>
<td>Special industry:</td>
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<td>Establishing on capital investment for the amount more than One billion and</td>
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<td>Providing direct employment to more than five hundred people for the whole year.</td>
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<td>Prevailing such industry:</td>
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<td>if increases installed capacity by twenty five percent and</td>
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<td>Make the capital to Rupees One billion and</td>
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<td>Provide direct employment for more than five hundred people for the whole year.</td>
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<td>Full income tax exemption up to five years and fifty percent for the three years thereafter from the date of commencement of transaction.</td>
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<td></td>
<td>Full income tax exemption up to five years and fifty percent for three years after on the income from capacity increment</td>
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<td>11(3)K(Ka)</td>
<td>Rebates for an industry established in a special economic zone.</td>
<td>Industry established in:</td>
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<td>Special economic zone situated in:</td>
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<td>Himali Districts and</td>
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<td>GON prescribed Hilly District.</td>
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<td>100% of applicable income tax for the 10 years from the date of commencement of transactions and 50% of the applicable income tax for the ensuing income years shall be exempt.</td>
<td></td>
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<tr>
<td>11(3)K(Kha)</td>
<td>Rebates for an industry established in a special economic zone.</td>
<td>Industry established in:</td>
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<td></td>
<td>Special economic zone situated in other region.</td>
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<td>100% of applicable income tax for the 5 years from the date of commencement of transaction and 50% of applicable income tax for the ensuing income years shall be exempt.</td>
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<tr>
<td>11(3)K(Ga)</td>
<td>Rebates on dividend distributed by industry established in a special economic zone.</td>
<td>Dividend distributed by:</td>
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<td>Industry established in special economic zone</td>
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<td>100% for the 5 years from the date of commencement of transaction and 50% for the ensuing 3 income years on applicable tax shall be exempt.</td>
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<tr>
<td>11(3)K(Gha)</td>
<td>Rebates for an industry established in a special economic zone.</td>
<td>Income earned by foreign investor in industry established in special economic zone from:</td>
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<td></td>
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<td>Foreign technology or</td>
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<td>Management service fee and</td>
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<td>Royalty</td>
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<td>50% of applicable income tax shall be exempt.</td>
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<tr>
<td>11(3)K(Nga)</td>
<td>Rebates on dividend distributed by industry established in a special economic zone.</td>
<td>Capitalization of accumulated profit through bonus share for expansion of capacity of:</td>
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<td>Special Industry,</td>
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<td>Agro-based industry or</td>
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<td></td>
<td>Industry related with tourism</td>
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<td></td>
<td>100% of applicable dividend tax shall be exempt.</td>
<td></td>
</tr>
</tbody>
</table>
| Section 11(3Kha) | Rebate for research and exploration of petroleum and natural gas | Conducting commercial operation within 2075 Chaitra by a person involved in transaction of research and exploration of 
- Petroleum and 
- Natural gas. | Full income tax for the first 7 years from the date of commencement of transaction and 50% of the income tax for 3 years thereafter will be exempted. |
|------------------|-------------------------------------------------|-------------------------------------------------|-------------------------------------------------|
| Section 11(3Ga) | Concession to various industries established in notified parks | Industry related with: 
- Software development, 
- Data processing, 
- Cyber café, 
- Digital mapping 
Established in 
- Technology park, 
- Biotech park and 
- Informational technology park 
Prescribed by GON through publishing in Nepal Gazette. | 50% of applicable tax will be exempted. |
| Section 11(3Gha) | Exemption and Concession to Licensed Person Engaged in generation, transmission or distribution of electricity. | i. Generation, transmission, or distribution of hydroelectricity by a person licensed for generation, transmission, distribution of electricity. 
ii. Similar facility will be available for electricity generated from solar, wind and bio product. 
But, 
iii. For a licensed person who has already commenced commercial operation at the time of introduction of this Sub Section. | full income tax for the first 10 years and 50% of the income tax for 5 years thereafter will be exempted From the date of commercial commencement within 2080 Chaitra 
Provision at time of getting the license will be applicable |
| Section 11(3Nga) | Concession on exports | On income earned from exporting goods manufactured by a manufacturing industry. | The rate of tax will be exempted by 25% |
| Section 11(3Cha) | Concession for an activity of construction and operation of an Infrastructure | On income earned: 
- From construction and operation of 
  - Road, 
  - Bridge, 
  - Airport, 
  - Tunnel and 
- From operating through investment in 
  - Tram, 
  - Trolleybus. | the rate of tax will be exempted by 40% |
| Section 11(3Chha) | Concession to Listed Companies | Entities listed in stock exchange which are 
- Production-oriented, 
- Tourism service, 
- Hydro electricity generation, distribution and transmission and 
- To the entities mentioned in Sub Section (3Ga) of Section 11. | tax will be exempted by 10% |
| Section 11(3Ja) | Concession to Liquors Manufacturing Industries | Fruit based industry established in very undeveloped area manufacturing 
- Brandy, 
- Cider and 
- Wine | 40% income tax will be exempted for 10 years from commencement of operation.
### Note:

1. A person eligible for more than one concession under Section 11 with respect to the same income shall be entitled to one concession of its own choice.

### Example:

A manufacturing co. (special industry) has been operating in under-developed area, total of 650 Nepalese citizens were employed in the industry for a whole year during the relevant income year. In such cases assessee have two options:

**Option 1:**

Tax Rate = 20% X 90% (Being employee more than 300) = 18%

**Option 2:**

Tax Rate = 20% X 30% (Being situated at underdeveloped areas) = 6%

Assessee should select Option 2.

2. While calculating the income by a person under subsections (1), (2), Clauses (Ka) and (Kha) of (3), (3Ka), (3Kha), (3Ga) and (3 Gha), Sub Section (13) , (14) and (15) of Section 1 of Schedule 1 and Sub Section (2), (3), (3Ka) and (4) of Section 2 of Schedule -1 shall calculate the income assuming the only income derived by a separate person.

### Example:

ABC Limited a manufacturing industry (Special Industry) has registered office situated at Kathmandu. It has another units situated at Dhadhing (Under developed Area). Total transactions of ABC Limited during income year 2072-73 is as follows: (In Thousand)

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Kathmandu</th>
<th>Dhadhing</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sales</td>
<td>21,000</td>
<td>14,000</td>
<td>35,000</td>
</tr>
<tr>
<td>COGS</td>
<td>15,000</td>
<td>12,500</td>
<td>27,500</td>
</tr>
<tr>
<td>Operating Expenses</td>
<td>1,000</td>
<td>800</td>
<td>1,800</td>
</tr>
</tbody>
</table>

Company has maintained separate books of account for both of the offices. However, company has incurred total expenses amounting Rs. 500,000 for both of the offices. Then total income and tax liability of company shall be as follows:

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Kathmandu</th>
<th>Dhadhing</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Amount to be included in income</td>
<td>21,000</td>
<td>14,000</td>
<td>35,000</td>
</tr>
<tr>
<td>Less: Deductible Expenses</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cost of Goods Sold</td>
<td>15,000</td>
<td>12,500</td>
<td>27,500</td>
</tr>
<tr>
<td>Operating Expenses</td>
<td>1,000</td>
<td>800</td>
<td>1,800</td>
</tr>
<tr>
<td>Indirect Expenses (In the ratio of sales)</td>
<td>300</td>
<td>200</td>
<td>500</td>
</tr>
<tr>
<td>Assessable Income</td>
<td>4700</td>
<td>500</td>
<td>5,200</td>
</tr>
<tr>
<td>Taxable Income</td>
<td>4700</td>
<td>500</td>
<td>5,200</td>
</tr>
<tr>
<td>Applicable Tax Rate</td>
<td>20%</td>
<td>6%</td>
<td></td>
</tr>
<tr>
<td>Tax Amount</td>
<td>940</td>
<td>30</td>
<td>970</td>
</tr>
</tbody>
</table>
1. EXAMPLE

i. Mr. Mukesh and his family member is engaged in agricultural business in land situated within ceiling prescribed in Land Act 2021. During an Income Year if he earned profit from such transaction amounting Rs. 5,00,000 then such income shall be exempt from tax.

ii. Annapurna Multipurpose Cooperative Society, a Cooperative Society registered under Cooperative Act, 2048 was established for development of agricultural business situated in Annapurna Himalayan Region. During accounting year 2072-73 if Cooperative Society earned profit amounting NRS. 10,000,000 then such income shall be exempt from tax.

iii. Concession available for special industry and information technology industry for

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Tax Rate for Special Industry (In %)</th>
<th>Tax Rate as per Section 11 (3) (Ka) (In %)</th>
<th>Tax Rate for Information Technology Industry (In %)</th>
<th>Tax Rate as per Section 11 (3) (In %)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Providing direct employment to 300 or more Nepalese Citizen</td>
<td>20</td>
<td>18</td>
<td>25</td>
<td>22.50</td>
</tr>
<tr>
<td>Providing direct employment to 1200 or more Nepalese Citizen</td>
<td>20</td>
<td>16</td>
<td>25</td>
<td>22.50</td>
</tr>
<tr>
<td>Providing direct employment to 100 or more Nepalese Citizen including at least 33% women, appressed and handicapped</td>
<td>20</td>
<td>16</td>
<td>25</td>
<td>25</td>
</tr>
</tbody>
</table>

iv. Concession to Special Industry established in various areas

<table>
<thead>
<tr>
<th>Place of industry</th>
<th>Tax Rate for Special Industry (In %)</th>
<th>Tax Rate as per Section 11 (3) (Kha) (In %)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Very Undeveloped</td>
<td>20</td>
<td>2</td>
</tr>
<tr>
<td>Undeveloped</td>
<td>20</td>
<td>4</td>
</tr>
<tr>
<td>Underdeveloped</td>
<td>20</td>
<td>6</td>
</tr>
</tbody>
</table>

The Institute would like to congratulate Council members Mr. Baburam Gautam and Mr. Jagannath Devekota for being honored, on the auspicious occasion of Republic Day, with SUPRAVAL JANA SEWA SHREE BIBHUSHAN for their outstanding performance in public service under the recommendation of Nepal Government.
Capital Gain Tax a Big Surprise to Many

NEPSE has reached the all-time highest and the real estate market has regained its momentum. Many new investors are entering into capital markets. Tax implication on these transactions are one big surprise for many. Most countries' tax laws provide for some form of capital gains taxes on investors' capital gains, although capital gains tax laws vary from country to country.

A capital gains tax is a type of tax levied on capital gains incurred by individuals and entity. Capital gains are the profits that an investor realizes when he or she sells the capital asset for a price that is higher than the purchase price.

Capital gains taxes are only triggered when an asset is realized, not while it is held by an investor. An investor can own shares that appreciate every year, but the investor does not incur a capital gains tax on the shares until they are sold.

A capital gains tax (CGT) is a tax on capital gains, the profit realized on the sale of a non-inventory asset that was purchased at a cost amount that was lower than
the amount realized on the sale. The most common capital gains are realized from the sale of stocks, bonds, precious metals (excluded in Nepal for natural person) and property.

Understanding Capital Gains Tax (CGT) under Income Tax Act, 2058 requires the understanding of types of assets considered by Income Tax Act, 2058. Income Tax Act, 2058 is based on the premise that assets are classified into five categories as shown below.

Trading Stock, Depreciable assets (in which depreciation is deducted) and Business Assets (all other assets of the business except Trading Stock and Depreciable Assets) are assets related to an entity/business of individual.

The two remaining classification relates to assets owned by individual and is not used for any business or investment.

Non-Business Chargeable assets are those assets other than trading stock, business assets or depreciable assets. There are assets owned by natural person. Income Tax Act, 2058 has given a special definition of Non-Business chargeable assets.

Non-Business Chargeable Assets mean lands, buildings and interest in any entity, or securities, other than the following assets:

1. Business assets, depreciable assets or trading stocks.
2. Private house of a natural person in the following conditions:
   (a) Under continued ownership for ten or more years, and
   (b) Lived in for ten or more years continuously or at different times by the person.

Explanation “private house means building and area covered by the building or one ropani of land whichever is lower”.

2a. An interest of a beneficiary in a retirement fund,
3. Land and private house of a natural person which has been disposed of at a price of less than three million rupees, or
4. Assets disposed of through transfer by any means other than sale and purchase within three generations.

Other Assets means assets other than trading stock, depreciable assets, business assets or non-Business chargeable assets and is not subject to tax. Example is gold held by an individual, land disposed at value less than NRs. 3 million. The gain or loss on these assets are not covered within the definition of income tax and is not taxable.

Therefore following types of disposal of land and buildings of natural person is not taxable

Therefore Income Tax Act, 2058 covers land and building and interest held in an entity excluding certain land and building and interest of a beneficiary in a retirement fund as non-business chargeable assets and capital gain tax is charged on it.
Other than this the land and building of natural person is taxable.

Further the same definition of non-business chargeable assets covers the interest held in any entity or securities. It means gain on disposal of shares, bonds, debentures or any kind of interest held in any company or entity is taxed. Only the interest held by beneficiary in any retirement fund is not covered by the definition of non-business chargeable assets.

Therefore, Income Tax Act, 2058 has covered land and building and interest held in any entity ie; shares, bonds etc. within the preview of capital gain tax is as follows.

**Table 1**

<table>
<thead>
<tr>
<th>TYPE Owned By</th>
<th>Classification of Assets</th>
<th>Period of Ownership</th>
<th>TDS (U/S 95KA)</th>
<th>Deducted by</th>
<th>Status</th>
<th>Final Applicable Tax (Schedule 1)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Natural Person</td>
<td>Non Business Chargeable Assets</td>
<td>Owned below 5 years</td>
<td>5%</td>
<td>(Land Revenue)</td>
<td>Non Final</td>
<td>5%</td>
</tr>
<tr>
<td>Natural Person</td>
<td>Non Business Chargeable Assets</td>
<td>Owned Above 5 years</td>
<td>2.50%</td>
<td>(Land Revenue)</td>
<td>Non Final</td>
<td>2.50%</td>
</tr>
<tr>
<td>Other Than Natural Person</td>
<td>Other than Non-Business Chargeable Assets and Other Assets</td>
<td></td>
<td>10%</td>
<td>(Land Revenue) Malpot</td>
<td>Non Final</td>
<td>Tax Rate Applicable to Concerned Business</td>
</tr>
</tbody>
</table>

The implication of capital gain tax on land and building is clarified in Table 1 above. In case of land and building owned by natural person, the land and building needs to be checked if it falls within the definition of non-business chargeable assets or not. If it comes within the definition of non-business chargeable assets (i.e. land having value of more than 3 million; land which is owned for less than 10 years), TDS is deducted by Land Revenue Office at the time of transfer of ownership on the value of gain. 5% TDS is deducted if its owned for less than five years and 2.5% is deducted if owned above five years.

Similarly, in case of land and building owned by any person other than entity, 10% TDS will be deducted by Land Revenue Office as per Financial Byelaws, 2073. Till 2072, the TDS is not required to be deducted by Land Revenue Office on land and building owned by Entities. In case of transfer of land and building from Borrower (natural person) to bank in the form of Non-Banking Assets, the Land Revenue Office is deducting TDS considering it as the TDS paid by the borrower.

**Table 2**

<table>
<thead>
<tr>
<th>TYPE Owned By</th>
<th>Listing</th>
<th>TDS (u/s 95KA)</th>
<th>Deducted by</th>
<th>Status</th>
<th>Final Applicable Tax (Schedule 1)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Interest in an Entity (i.e. Shares)</td>
<td>Natural Person</td>
<td>Listed in Stock Exchange</td>
<td>5%</td>
<td>Broker</td>
<td>Non Final</td>
</tr>
<tr>
<td>Interest in an Entity (i.e. Shares)</td>
<td>Natural Person</td>
<td>Not Listed in Stock Exchange</td>
<td>10%</td>
<td>Concerned Entity</td>
<td>Non Final</td>
</tr>
<tr>
<td>Interest in an Entity (i.e. Shares)</td>
<td>Other Than Natural Person except mutual fund</td>
<td>Listed in Stock Exchange</td>
<td>10%</td>
<td>Broker</td>
<td>Non Final</td>
</tr>
<tr>
<td>Interest in an Entity (i.e. Shares)</td>
<td>Other Than Natural Person except mutual fund</td>
<td>Not Listed in Stock Exchange</td>
<td>15%</td>
<td>Concerned Entity</td>
<td>Non Final</td>
</tr>
</tbody>
</table>
The effect of capital gain tax on interest in an entity is clarified in Table 2 above. In case of disposal of interest of an entity listed in stock exchange, 5% TDS is deducted by stockbroker for stocks owned by Natural Person and 10% for stocks owned by an entity. Similarly if the gain is made on the stocks not listed in Stock Exchange, the concerned entity whose stocks are sold is entitled to deduction of TDS which is 10% for natural person and 15% for entity. As per the Finance Act, 2073, the company registrar is required to record the transfer of shares only after the submission of proof of deposit of TDS on gain of such transfer. Earlier such proof is not mandatory. Here the logic may be that all transfer needs to have gain. However, in practice, the shareholder may sell shares at price below he has purchased. The enforcement of this Clause is yet to be tested.

The TDS deducted in disposal of land and building nor the disposal of shares are final withholding. The natural person or entity both is required to submit tax return.

In Nepal, individuals and entity are subject to capital gains taxes on their annual net capital gains. Therefore, the entity and natural person both are allowed to calculate net capital gains reducing capital losses incurred during the year and pay taxes on the net capital gains. It is important to note that net capital gains are subject to tax because if an investor sells two stocks during the year, one for a profit and an equal one for a loss, the amount of the capital loss incurred on the losing investment will counteract the capital gains from the winning investment. In this situation, the investor will have surplus TDS deducted on the profitable investment which can be carried forward infinitely.

The entity will be taxed at the normal tax applicable to the entity and any TDS deducted earlier is allowed to be deducted on the total amount to be paid. Therefore, effectively there is no concept of Capital Gain Tax in case of person other than natural person. Any gain on assets related to business (trading stock, depreciable assets, business assets) is taxed on the applicable tax rate of the concerned entity. For example if the gain is made on sale of land used by any bank, it is taxed at 30%, any trading company at 25% tax rate, and special industry at 20%.

Similarly in case of natural person, they are allowed to utilize the benefit of first slab and deduct TDS on the remaining amount. This is clarified from following example:

<table>
<thead>
<tr>
<th>Bank</th>
<th>Particulars</th>
<th>Natural Person</th>
</tr>
</thead>
<tbody>
<tr>
<td>9,000</td>
<td>Land Sold below 5 yrs (net incomings)</td>
<td>9,000</td>
</tr>
<tr>
<td>7,800</td>
<td>Cost Price (net outgoings)</td>
<td>7,800</td>
</tr>
<tr>
<td>1,200</td>
<td>Gain</td>
<td>1,200</td>
</tr>
<tr>
<td>120</td>
<td>TDS Deducted by Land Revenue Office</td>
<td>60</td>
</tr>
<tr>
<td>360</td>
<td>Total Tax Liability</td>
<td>42.5</td>
</tr>
<tr>
<td>120</td>
<td>TDS Deducted</td>
<td>60</td>
</tr>
<tr>
<td>240</td>
<td>Yet to Be Paid/(excess)</td>
<td>(17.5)</td>
</tr>
</tbody>
</table>

In the given example in Table 3 both the bank and natural person have gained the same amount of profit from sale of land. The Land Revenue Office will deduct TDS at 10 percent in case of bank while 5% in case of natural person as the land is sold within 5 years. As normal tax is applicable for any entity, the bank is required to pay tax at 30% on the gain which amounts to NRs. 360 thousands in which the TDS deducted by Land Revenue Office amounting to NRs. 120 thousands can be set off as advance tax. While submitting the tax return, the natural person can claim benefit of tax slab. As social security tax is applicable only to natural person having remuneration income, no tax is applicable to natural person (opting single) for amount up to NRs. 350 thousand from FY 2073/74. (NRs.250,000 for FY 2072/73). The remaining amount of NRs. 850 thousand is taxed at 5% as capital gain tax. The concerned natural person can claim with
Inland Revenue Department for refund of NRs. 17.5 thousand so paid in excess within two years under Section 113 of Income Tax Act, 2058.

But in practice, the cases of filing of return by natural person for transaction in shares, land and building is very few. Many does not have knowledge of the requirements. Further, Inland Revenue Department has also not published this fact for the awareness of tax payer. It may be because of the fact that the claim for refund will increase dramatically.

Conclusions
The TDS deducted in disposal of land and building nor the disposals of shares are final withholding. The natural person or entity both is required to submit tax return.

Effectively there is no concept of Capital Gain Tax in case of person other than natural person. They are taxed at tax rate applicable to concerned entity.

References
- Income Tax Act, 2058
- Finance Act, 2073
- Notice Issued by Inland Revenue Department, on capital Gain on non-business chargeable assets (Land and Building)
- Inland Revenue Department Directives regarding Capital Gain on Disposal of Land and Land & Building, 2072
Revenue mobilization has a crucial role in fiscal policy implementation, especially in a developing country where the demand of public funds for public expenditure is high. Tax revenue is a better source of resource mobilization than the other sources such as deficit financing and money creation. As tax revenue is the major source of domestic revenue in Nepal, the measurement of tax buoyancy and elasticity would be very beneficial in terms of reforms in tax structure as well as revenue administration. In addition to this, the study of tax buoyancy and elasticity is also useful for revenue forecasting. Tax buoyancy and elasticity estimates are the dynamic tools for measuring the tax performance.

Tax revenue may change due to a variety of factors, such as changes in income, changes in tax rate and tax base, changes in efficiency of tax assessment and collection, among others. The responsiveness of tax revenue to such changes can be explained with the help of tax buoyancy and elasticity.

**Tax buoyancy** is an indicator to measure efficiency and responsiveness of revenue mobilization in response to growth in the Gross Domestic Product (GDP) or National Income. Tax buoyancy measures the total response of tax revenues to changes in national income. It takes into account both the effect of increases in income
and discretionary changes on the revenues from a tax. Discretionary tax changes are under the control of tax authorities. They are due to changes in tax rates, base definition, and collection and enforcement procedures. Non-discretionary changes arise from the natural growth of economy.

Tax buoyancy is a measure of both the soundness of the tax bases and the effectiveness of past tax changes in terms of revenue collection. A tax which is buoyant is one whose revenues increase by more than one percent for a one percent increase in national income or output.

Tax buoyancy can be expressed as follows:

\[ E_{TY}^b = \frac{\Delta T^b \cdot Y}{\Delta Y \cdot T^b} \]

- \( E_{TY}^b \) = Buoyancy of tax revenue to income
- \( T^b \) = Total tax revenue
- \( \Delta T^b \) = Change in total tax revenue
- \( Y \) = Income
- \( \Delta Y \) = Change in income

Buoyancy is reduced if tax exemptions or tax rates are lowered over time. Buoyancy may also be low if the fundamental tax elasticity of tax system is low.

**Tax Buoyancy in Nepal**

There is a strong connection between the government’s tax revenue earnings and economic growth. The simple fact is that as the economy achieves faster growth, the tax revenue of the government also goes up. Tax buoyancy explains this relationship between the changes in government’s tax revenue growth and the changes in GDP. It refers to the responsiveness of tax revenue growth to changes in GDP.

As per annual report of IRD for FY 2070/71, taking year of implementation of Modern Tax System FY 2058/59 as the base year, the ratio of total revenue to total GDP was 11% in comparison to around 6.1% in initial years. With the development in Nepalese economy, the ratio improved to 15.3% in FY 2066/67 but again dropped to 14.6% in FY 2067/68. The ratio rises remarkably to 15.6% in FY 2068/69 and 17.5 in FY 2069/70 and highest 18.1% in FY 2070/71. The ratio of total tax revenue to total GDP was 16.1% in FY 2070/71.

**Figure 1: Ratio of Tax Revenue to GDP**

**Figure 2: Ratio of Excise, Income Tax and VAT to GDP**

Hence, tax buoyancy shows the association between economy’s performance and the government’s tax revenue. It indicates the high sensitiveness of tax revenue realization to GDP growth. Here the tax buoyancy is higher for indirect taxes i.e. tax based on consumption of goods and services. The heavy emphasis on trade and consumption taxes coupled with a lesser reliance on income and property taxes is common in developing countries. As per Annual report of IRD for FY 2070/71, the total contribution to total revenue of VAT is 32%, Income tax is 25%, customs is 22% and excise is 15%.
**Tax Elasticity**

Tax elasticity measures the pure response of tax revenues to changes in the national income. It reflects only the built-in responsiveness of tax revenue to movement in national income.

The tax elasticity calculation excludes the impact of changes in tax rates and tax bases. It considers only the effects due to changes in income levels, whether or not changes were made in the tax structure during that time period. The value of the tax elasticity gives an indication to policy-makers of whether tax revenues will rise at the same pace as the national income.

Tax elasticity, \( E_T = \frac{\% \text{ change in tax revenue}}{\% \text{ change in GDP}} \)

\[ \frac{(dT/T)/(dGDP/T)} {dT/T} \]

The elasticity of import tax is 0.54 implying that a 10 percent change in the nominal GDP results in a 5.4 percent change in import tax.

Personal income tax can be quite elastic if the exemptions and deductions are limited. As more income grows, more tax payers become subject to income tax and also people already in the system pay higher average taxes.

Elasticity of indirect taxes depends mainly on two factors.

- The type of tax, i.e. whether it is a unit tax or an ad valorem (percentage) tax. As nominal GNP increases due to the general rate of inflation the revenue from a unit tax remains constant in nominal value. This means that real tax revenue will fall. This causes a decrease in the ratio of tax revenue to GNP. The tax revenue from a percentage (ad valorem) tax would increase in the same proportion as the price level.

- The growth in demand of certain goods and services may not increase at as fast a rate as the national income.

As the per capita income of a country increases the income elasticity of each of the goods and services will change. As per capita income increases with economic development, the demand for government goods and services such as transportation, communication, and general government administration services also increases.

For the indirect tax system to have a tax elasticity of greater than one its base will have to include a large proportion of goods and services that have income elasticity of demand greater than 1.

Since elasticity is an important element of taxation in a developing economy, it is crucial that policy makers be able to identify those taxes which are elastic and those which are inelastic. Increasing the overall elasticity of the tax system involves utilizing more heavily those taxes which are most elastic. Further, the elasticity of individual taxes can be increased by certain measures. One is by improved administration. Taxes which are better administered tend to be more elastic. Another measure is to convert specific excise taxes to ad valorem taxes. Since an ad valorem tax applies a rate to the base, revenues from ad valorem taxes tend to grow with the economy without the need for discretionary increases.

**Advantages of Elastic Tax System**

- An elastic tax system is desirable in a developing economy because it means that Tax revenue grows proportionately faster than income making it possible to fund growing demands for government services without politically sensitive tax increases. Unless tax rates are increased inelastic taxes will decline in revenue importance in the tax system over time.

- An elastic tax system is better automatic stabilizer than inelastic one. An elastic system is likely to be progressive, perhaps helping meet vertical equity goals. A progressive tax system has elasticity greater than one.
Disadvantages of Elastic Tax System

- An elastic tax system may promote too high rate of government growth. Revenues that are available tend to be spent rather unwisely.
- Revenues from elastic tax system tend to be volatile making planning difficult.

Difference between Tax Buoyancy and Tax Elasticity

The concepts of tax buoyancy and tax efficiency are used to measure the responsiveness of tax revenue to economic growth. Tax elasticity may be defined as the ratio of a percentage change in adjusted tax revenue to a percentage change in income i.e. nominal GDP. On the other hand, tax buoyancy refers to changes in actual tax revenues due to the changes in income as well as due to the changes in discretionary measures such as tax rates and tax bases.

Tax buoyancy is a crude measure which does not distinguish between discretionary and automatic growth of revenue. When no attempt is made to control discretionary rate or base changes, then the responsiveness of tax revenue to a change in GDP is called tax buoyancy. When an attempt is made to control discretionary changes, the measure of responsiveness of tax is called tax elasticity.

Elasticity is a preferred measure of tax responsiveness since it controls for automatic revenue changes. Although tax buoyancy is a useful tool for the purposes of policy design, the income or GDP based revenue-forecasting models rely on tax elasticity for estimating future tax revenue collections based on the current tax system.

This distinction between the tax elasticity and buoyancy is very useful in analyzing and evaluating whether future revenues will be sufficient to meet the resource needs without changing the rates or bases of the existing tax. To measure the tax elasticity, historical tax series must be adjusted so as to eliminate the effects of tax revenues from discretionary changes. If there is no change in the tax rates and the tax base during the reference period, the buoyancy will be the same as elasticity.

For policy purposes, it is usually useful to distinguish between revenue growth due to discretionary changes and revenue growth due to changing economic conditions. Tax elasticity is a measure designed for this purpose since it measures the responsiveness of tax revenue to a change in national income or output after controlling for exogenous influences such as discretionary changes in tax policy. If a tax is elastic, a one percent increase in GNP or GDP results in a greater than one percent increase in revenue from the tax holding constant for discretionary tax changes.

However, for various reasons, studies of tax responsiveness often focus on tax buoyancies rather than tax elasticity. One problem is in obtaining information on discretionary revenue changes. Sometimes this information is available through the Minister of Finance; however this source may not know or be willing to report the discretionary revenue change. At best, the information is an estimate which may or may not be based on a sound economic model. Secondly, utilizing information on discretionary revenue changes to control for such changes may result in the loss of degrees of freedom in a regression analysis. This is a particular problem in the study of developing economies since the data series are usually short to begin with. Each new control variable reduces the number of degrees of freedom by one, reducing the efficiency of the regression estimates.

A study by Nepal Rastra Bank for tax elasticity and buoyancy in Nepal for the period of 1975 to 2005 (applying time series regression approach for empirical measurement) has revealed that the tax system in Nepal is inelastic in the period 1975-2005 with a more than unitary buoyancy coefficient, thus reflecting that the bulk of revenue collection emanates from discretionary changes in the tax, rather than from automatic responses.
Fiscal jurisdiction is one of the most seriously protected jurisdictions of a country. In this regards, double taxation continues to be one of the major complications to the development of international economic relations.

Double taxation is the levying of tax by two or more jurisdictions on the same declared income (as income taxes), asset (as capital taxes), or financial transaction (as sales taxes).

As a tax payer's own country (i.e home country) has a sovereign right to tax him, the source of income may be in some other country (i.e host country) which also claims a right to tax the income arising in that country. Such a situation creates double liability to the person carrying on the activities in two different tax system. This double liability is often mitigated by tax treaties between countries. Such a agreement is known as “ Double Taxation Avoidance Agreement.” Countries are often forced to discuss and settle the claims of other countries by means of double taxation avoidance agreements, in order to bring down the barriers to international trade. These treaties are based on the general principles laid down in the model draft of the Organisation for Economic Cooperation and Development (OECD) with suitable modifications as agreed to by the other contracting countries.

Every country seeks to tax the income generated within its territory on the basis of one or more connecting
factors such as location of the source, residence of taxable entity and so on. This creates interaction of tax payer with two tax system of different countries resulting in double taxation. Nepal has also imposed Income Tax on the “Total income earned outside Nepal i.e. income earned anywhere in the world”. The result is that income arising to a resident out of Nepal is subjected to tax in Nepal and, also in host country which provides the source for that income. Double tax treaties are settlements between two countries, which include the elimination of international double taxation, promotion of exchange of goods, persons, services and investment of capital.

The statutory authority to enter into such agreements is vested in the Government of Nepal by the provisions contained in Section 73 of the Income Tax Act in terms of which Nepal has entered into agreements of this nature which deal with different types of income which may be subjected to double taxation.

Sec – 73 of Income tax Act 2056 states

(1) In cases where any income of any person is taxable pursuant to this Act or the laws in force and the same income is also taxable in a foreign country, Government of Nepal may conclude an international agreement with the foreign country for the avoidance of double taxation.

(2) This Sub-section shall be applicable in cases where, pursuant to any international agreement concluded with Nepal, the competent authority of the other country requests the Department to collect in Nepal the amount payable by any person who is in arrears of that amount, pursuant to the taxation law of that other country.

(3) In cases where Sub-section (2) is applicable, the Department may, for the purpose of sending that amount to that competent authority, send a notice in writing to the person who is in arrears of tax and require him to pay such amount to the Department within the date mentioned in that notice.

(4) This Sub-section shall be applicable in cases where any international agreement contains a provision under which Nepal has to exempt income or payment or has to apply the reduced tax rate to income or payment.

There are currently 10 agreements which Nepal has entered into the double taxation avoidance agreement with other countries. A list of such agreements are given below.

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<th>Agreement</th>
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<td>Double taxation Treaty India</td>
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<td>2</td>
<td>Double taxation Treaty China</td>
</tr>
<tr>
<td>3</td>
<td>Double taxation Treaty Austria</td>
</tr>
<tr>
<td>4</td>
<td>Double taxation Treaty Korea</td>
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<td>Double taxation Treaty Mauritius</td>
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<td>Double taxation Treaty Sir Lanka</td>
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<td>10</td>
<td>Double taxation Treaty Thailand</td>
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There are different models for Double Taxation Avoidance Agreement but agreement are categorised on the basis of scope

a. Comprehensive agreement : Its scope addressed to all sources of income earned by the tax payer. Comprehensive agreements ensure that the taxpayers in both the countries would be treated equally, in respect to problems relating to double taxation.

b. Limited agreement : Scope only cover
   ♣ Income from operation of aircrafts & Ships
   ♣ Estates
   ♣ Inheritance
   ♣ Gifts

The Double Taxation Avoidance Agreement facilitates the settlement of the tax claims between two governments, both legitimately interested in taxing a particular source
of income. Such a agreement helps in avoiding the burden of international double taxation, by

a) Defining and adopting the rules for division of revenue between two countries;
b) exempting certain incomes from tax in either country;
c) reducing the applicable rates of tax on certain incomes taxable in either countries

Furthermore, it helps a taxpayer to know with greater certainty the potential limits of his tax liabilities.

As the principle of Double taxation agreement is to share the revenue between two countries, tax treaties allocate jurisdiction to the concerned countries, with respect to the right to tax a particular kind of income. The agreements provide of allocation of taxing jurisdiction to different contracting parties in respect of different source of income. In double taxation avoidance treaty of Nepal with other countries, the rules include that income is taxed as follow

a. Income From Immovable Property:
   Income derived from immovable property may be taxed in the contracting state where the immovable property is situated. It is applicable for all the DTAA currently signed by Nepal.

b. Business Profits
   The profits of an enterprise of a Contracting State shall be taxable where the enterprise is resident unless the enterprise carries on business in the other Contracting State through a permanent establishment situated therein. It is applicable for all the DTAA currently signed by Nepal.

c. Shipping And Air Transport
   Profits from the operation of ships or aircraft in international traffic shall be taxable only in the Contracting State in which the place of effective management of the enterprise is situated. It is applicable for all the DTAA currently signed by Nepal.

d. Associated Enterprises
   Where a Contracting State includes in the profits of an enterprise of that State-and taxes accordingly-profits on which an enterprise of the other Contracting State has been charged to tax in that other State and the profits so included are profits which would have accrued to the enterprise of the first-mentioned State if the conditions made between the two enterprises had been those which would have been made between independent enterprises, then that other State shall make an appropriate adjustment to the amount of the tax charged.

e. Dividends/Interest/Royalty
   Dividends/Interest/Royalty paid by a company to a resident of the other Contracting State may be taxed in that state where receiver is resident. However, it can be taxed by source contracting state but the rate of tax should be as per the Double taxation avoidance agreement.

f. Capital Gains
   Gains derived from alienation of immovable property may be taxed in the contracting state where the immovable property is situated. It is applicable for all the DTAA currently signed by Nepal.

g. Independent Personal Services
   Income derived by a resident of a Contracting State in respect of professional services or other activities of an independent character shall be taxable only in the state where he is resident unless he has a fixed base regularly available to him in the other Contracting State for the purpose of performing his activities or he is present in that other State for a period or periods exceeding in the aggregate 183 days( 90 days in
h. **Dependent Personal Services**

Salaries, wages and other similar remuneration derived by a resident of a Contracting State in respect of an employment shall be taxable only in the state where he is resident unless the employment is exercised in the other Contracting State. If the employment is so exercised, such remuneration as is derived therefrom may be taxed in that other State. It is applicable for all the DTAA currently signed by Nepal.

i. **Directors' Fees**

Director's fees and other similar payments derived by a resident of a Contracting State may be taxed in that State where the company is resident. It is applicable for all the DTAA currently signed by Nepal.

j. **Artistes And Sportsmen**

Income derived by a resident of a Contracting State as an entertainer, from his personal activities exercised in the other Contracting State, may be taxed in that State. It is applicable for all the DTAA currently signed by Nepal.

k. **Pensions And Social Security Payments**

Pensions and other similar remuneration paid to a resident of a Contracting State in consideration of past employment may be taxed in that State where receiver is resident. However, such pensions and other similar remuneration may also be taxed in the other Contracting State if the payment is made by a resident of that other State or a permanent establishment situated therein.

l. **Government Service**

Remuneration, other than a pension, paid by a Contracting State or a political subdivision or a local authority thereof to an individual in respect of services rendered to that State or subdivision or authority shall be taxable only in that State. It is applicable for all the DTAA currently signed by Nepal.

m. **Teachers And Researchers**

A professor, teacher or researcher who makes a temporary visit to a Contracting State for the purpose of teaching or conducting research at a university, college, school or other recognized educational institution and who is, or immediately before such visit was, a resident of the other Contracting State shall be exempted from tax in the first-mentioned State for a period not exceeding two years in respect of remuneration for such teaching or research. However, there is no such provision in DTAA with Austria, Norway, Pakistan, and Thailand.

n. **Students And Trainees**

An individual who, immediately before visiting a Contracting State, was a resident of the other Contracting State and whose visit to the first mentioned Contracting State is solely for the purpose of studying, training, carrying out research is a recipient of a grant, allowance or award from a governmental, religious, charitable, scientific, literary or educational organisation, shall be exempt from tax in the first-mentioned State. However, exemption for income from personal services from Sri Lanka, Quatar, and Korea has been limited by its DTAA.

There are various methods in tax treaties to avoid the effect of double taxation in international trade. They include

(i) **Exemption Method:**

This method is for the residence country to exclude foreign income from its tax base so that the exclusive right to tax such incomes goes to the source country. This is known as complete exemption method and is
sometimes followed in respect of profits attributable to foreign permanent establishments or income from immovable property.

(ii) Credit Method:

As the resident of the countries remains liable in the country of residence on its global income, credit for tax paid in the source country is given by the residence country against its domestic tax as if the foreign tax were paid to the country of residence itself.

(iii) Tax Sparing:

In order to promote foreign investment flows in developing countries from foreign developed countries, the investors are provided with the benefit of tax incentives to preserve such investments. This is done through the Tax Sparing method, where the tax credit is allowed by the country of its residence, not only in respect of taxes actually paid by it in country but also in respect of those taxes country forgoes due to its fiscal incentive provisions under the Income Tax Act (ITA).

The regular tax credit is a measure of preventing double taxation, but the tax sparing credit extends the relief granted by the source country to the investor in the residence country by the way of an inducement to stimulate foreign investment flows and does not seek reciprocal arrangements by the developing countries.

Applicability of Treaty benefits:

Resident

Double tax avoidance treaty would be applicable to those person who qualify in terms of the treaty as a residence of a person.

Since the taxability of income depends upon the residential status, the determination of the residential status of the tax payer is of great significance. To get the benefit of tax treaty only the person who is resident of a contracting state can seek relief from double taxation. The treaty provision determines whether a person is a resident of a contracting state.

The double tax avoidance treaty, 'resident of contracting state' means any person who, under the laws of that State, is liable to tax therein by reason of his domicile, residence, place of management or any other criterion of a similar nature, and also includes that State and any political subdivision or local authority thereof. This term, however, does not include any person who is liable to tax in that State in respect only of income from sources in that State

If an individual is a resident of both Contracting States, then his status shall be determined as follows:

a) he shall be deemed to be a resident only of the State in which he has a permanent home available to him; if he has a permanent home available to him in both States, he shall be deemed to be a resident only of the State with which his personal and economic relations are closer (centre of vital interests);

b) if the State in which he has his centre of vital interests cannot be determined, or if he has not a permanent home available to him in either State, he shall be deemed to be a resident only of the State in which he has an habitual abode;

c) if he has an habitual abode in both States or in neither of them, he shall be deemed to be a resident only of the State of which he is a national;

d) if he is a national of both States or of neither of them, the competent authorities of the Contracting States shall endeavor to settle the question by mutual agreement.

It first considers a person's liability to tax as a resident under the respective taxation laws of the state. If a person is a resident of both the contracting states, the residence would be determined in a state where he has permanent home or his personal or economic relation are closer.
or habitual abode or nationality and at last by mutual agreement

**Permanent Establishment:**

Double taxation treaties restrict the authority of the contracting states to tax business income of a foreign enterprise if such enterprise carries on business in Nepal through a permanent establishment. The term "permanent establishment" as defined in Article 5 means “a fixed place of business through which business of an enterprise is carried on.”

The definition requires performance of business activity through a fixed place of business in another country.

**The term "permanent establishment" encompasses**

a) a building site, construction, assembly or installation project, or an installation or drilling rig or ship used for the exploration or development of natural resources, including supervisory activities in connection therewith, but only if that site, project, or use lasts or those activities last more than six months;

b) the furnishing of services, including consultancy services, by an enterprise through employees or other personnel engaged by the enterprise for such purpose, but only where activities of that nature continue (for the same or a connected project) within the country for a period or periods aggregating more than 183 days within any twelve month period.

The first part suggests the existence of a fixed place of business, whereas the second part states that the business is carried on through a fixed place. If any of the part is not available then there is no permanent establishment.

**Treaty shopping:**

Treaty Shopping generally refers to a situation where a person, who is resident in one country (home country) and who earns income or capital gains from another country (Source country), is able to benefit from a tax treaty between the source country and yet another country (Third country). This situation often arises where a person is resident in the home country but the home country does not have a tax treaty with the source country. The basic feature of treaty shopping is to establish base companies in other states solely for the purpose of enjoying the benefit of particular treaty existing between the state involved and the third state.

For example, a Nepal pvt Ltd resident in the Nepal (the home country) may own a Corporation (“ABC Corporation”) in the U.S. (the source country). Dividends paid from ABC Corporation to Nepal Pvt Ltd would be subject to a 30% U.S. withholding tax. If Nepal Pvt Ltd were to form a corporation (“XYZ Plc”) in the U.K. (the third country) and transfer the stock of ABC Corporation to XYZ Plc, dividends would be paid from ABC Corporation to XYZ Plc and, without anti-treaty shopping rules, these dividends would qualify for benefits under the U.S.-U.K. Income Tax Treaty.

If this approach were successful, the dividend withholding tax of 30% on dividends paid by ABC Corporation could be reduced to zero. In addition, because the U.K. does not impose any withholding taxes on dividends paid to non-U.K. residents, the overall tax rate of the group may decrease.

Different countries counter attack the problem of treaty shopping in different ways. The U.S. generally includes in its tax treaties with other countries specific rules that limit the benefits under the treaty in certain circumstances. These rules are typically called “limitation on benefits” or “LOB” provisions. This rule provides a set of objective tests that have to be satisfied as a primary condition before applying the tax treaty to a given transaction. Such a specific rule will address a large number of treaty-shopping situations based on the legal nature of, ownership in, and general activities of taxpayers intending to take advantage of the tax treaty.
Other countries, such as Nepal generally rely on domestic law anti-treaty shopping provisions, rather than including the rules within the treaty itself. Domestic law anti-treaty shopping rules are often implemented by providing that only “beneficial owners” of the payments are entitled to treaty benefits.

However, Nepal Tax Act Sec. 73(5) contains an anti-treaty shopping rules that allows Inland Revenue Department to restrict treaty benefit to any company if 50% or more underlying ownership of that company is not held by residents of that country.

Sec 73(5) of Income tax Act 2056 states

In cases where Sub-section (4) is applicable, any of the following entity shall not be entitled to enjoy tax exemption or tax deduction facility:-

(a) An entity who is considered as a resident of the other party of the agreement for purposes of the agreement, and

(b) Where Fifty percent or more portion of the vested ownership of that entity is owned by natural persons or by the entities in which any natural person has no interest and, for purposes of the agreement, the persons or entities are residents of both Nepal and of the other country party to the agreement.

Tax Haven:

Tax Haven are the place, in which certain taxes are imposed either at a low rate or not at all, is the best possible way out for those interested in reducing their tax rates.

In some countries, high tax rates can deter the tax payers and lead them to relocate to areas with comparative lower tax rates. This gives rise to tax competition among different governments. There are many Tax Haven specified for different types of tax as well as for different groups of people and companies. It has the potentiality to transform the tax structure of any nation. As a result, there are also some effective tax laws regulating the protections of the Tax Haven such that there are no revolution, changes or misuses within the economy.

There are some specific characteristics as being identified by the Organization for Economic Co-operation and Development (OECD) to decide the tax structure of any nation to be denoted as Tax Haven.

These are –

• Regarding the situations when there is either payment of no/only nominal taxes. In special cases Tax Haven creates such conditions to offer themselves as shelters for the non-residents to evade high taxes in their respective residential countries.

• Tax Haven generally stresses on protecting the personal financial information of the taxpayers. They have specific laws for the benefit of corporate houses and individuals that can protect them from the scrutiny and other strict laws of the foreign authorities.

The Income Tax Act, 2056 governs taxation of income in Nepal. According to section 6 of the Income Tax Act, residents of Nepal are taxable on their worldwide income, and non-residents are taxed only on income that has its source in Nepal.

The Income Tax Act of Nepal favors source-based taxation as compared to the OECD model conventions or treaties entered into by many developed countries that favor residence based taxation.

The policy adopted by the government of Nepal in regard to double taxation treaties is as follows:

• Foreign trade should be relieved of Nepalese taxes considerably so as to promote its economic and industrial development

• There should be co-ordination taxation with foreign tax legislation for Nepalese as well as foreign companies trading with Nepal

• The agreements are intended to permit the Nepalese
authorities to co-operate with the foreign tax administration.

Nepal primarily follows the UN model convention and one therefore finds the tax-sparing and credit methods for elimination of double taxation in most Nepalese treaties as well as more source-based taxation in respect of the articles on 'royalties' and 'other income' than in the OECD model convention.

Conclusion:
The regime of international taxation exists through bilateral tax treaties based upon model treaties, developed by the OECD and the UN, between the Contracting States. Nepal adopted the UN model convention and therefore finds the tax-sparing and credit methods for elimination of double taxation in most Nepali treaties as well as more source-based taxation in respect of the 'royalties' 'interest' and 'other income' than in the OECD model convention. Nepal is stepping into a network of tax treaties with various countries to facilitate free flow of capital into and from Nepal. However, the international tax regime has to be restructured continuously so as to respond to the current challenges and drawbacks.
Taxing Mergers & Acquisitions in Nepal

Introduction

Mergers and Acquisitions (M&A) are transactions in which the ownership of one entity, business organizations or their operating units are transferred to another entity or combined. As an aspect of strategic management, M&A allows enterprises to grow, shrink, change the nature of their business or improve their competitive position.

The term 'Mergers' and 'Acquisitions' are often used interchangeably. However, there are differences. While merger means unification of two into one, acquisition involves one entity buying out another and observing the same. From economic stand point both the Merges and Acquisitions result in the consolidation of assets and liabilities under one entity and the distinction between the both is less clear. Nepal Accounting Standard on Business Combination (NAS 21) calls Seller as 'Acquiree' and Buyer as 'Acquirer'. There are several advantages in M&A – cost cutting, efficient use of resources, acquisition of competence or capability, tax advantage and avoidance of competition are among the few.

Income Tax Act of Nepal does not define the Term 'Merger' and 'Acquisition'. However, it has referred Mergers and Acquisition as the Amalgamation of two or more Companies to become one. Income Tax Act of Nepal refers the term 'Mergers' in Section 47A for the Mergers of entities doing banking or insurance business.

Mergers and Acquisition covers basically three tax aspects, taxability
of assets and liabilities of Acquiree Company, Taxability to the Shareholders of Acquiree Company and the Treatment of assets and liabilities of Acquiree Company in the books of Acquirer Company. In the Nepalese context, Income Tax Act has discouraged the concept of Merger and Acquisition except for the entities doing Banking or Insurance Business.

A. Tax Implication of Mergers and Acquisition of entities doing other than Banking and Finance Business or Insurance Business

While the Mergers and Acquisition bring synergy after the merger by creating economics of scale, creating new market, avoiding competition to name a few. The impact of tax on the economics of Mergers and Acquisition transaction may be huge to both the Acquirer and Acquiree Company.

Tax Implications on the Acquiree Company

There are two basic implications of M&A to the Acquiree Company. First being the tax implication of M&A on Assets and Liabilities of the Acquiree Company and second the tax implication to the shareholders of the Acquiree Company. The question remains whether the Assets and Liabilities being amalgamated to the Acquirer Company constitutes disposal of Assets and Liabilities. If the same is considered disposal than what would be the incoming and outgoing for the purpose of calculating net gain/loss on such disposal of assets and liabilities. Similarly, in case of Shareholder of Acquiree Company, the shareholders will either get cash or shares of Acquirer Company in consideration to their shares held in Acquiree Company and whether such replacement constitute disposal for the purpose of Income Tax Act.

As per Section 40 of Income Tax Act, Sub Section (1), "If the ownership of any person over any property ceases, he shall be deemed to have disposed that property. The disposal of property has to include acts such as distribution of the property by the owner of the property, amalgamation of the property in other property or liability, sale of the property in installments or lease out to any other person under a financial lease, cancellation, destroy, loss, expiration or surrender of the same."

Sub Section (2) "If the burden of liability of any person ceases, he shall be deemed to have disposed that liability. The disposal of liability has to include acts such as settlement, cancellation, release and completion of the liability or amalgamation of liability in other liability or property"

From the above provision, it is clear that in the event of transfer of shares from Acquiree Company to Acquirer Company in any scheme of merger, the assets and liabilities of Acquiree Company is deemed to be disposed off by virtue of Section 40(1) & 40(2) of Income Tax Act. But interestingly Section 41 of Income Tax Act prescribes the manner for the disposal under clauses (c), (d), (e) & (f) of Sub Section 3 of Section 40, however it does not prescribe the manner in which disposal under Section 40(1) and 40(2) has to be done.

There is one view that for the purpose of computation of tax on such disposal under Section 40(1) & 40(2), Market Value of Assets or Liabilities will be considered as Incoming and Net Expenses incurred in such Assets or Liabilities will be considered as outgoing. Such tax should be paid by the Acquiree Company. However, to substantiate such view, there is no any clear provision in the Income Tax Act of Nepal.

The other view which the writer believes is that in the event of disposal of assets and liabilities because of merger, Section 47 of the Income Tax Act Applies. By virtue of Section 47, such assets and liabilities will be disposed off at the Value of Net Expenses incurred for the Assets and Net Income Earning for the Liabilities. Which suggest that the Assets and Liabilities will be disposed at Book Value and there will not be any tax liability on such disposal of assets and liabilities of Acquiree Company.
Taxability to the Shareholders of Merged/Acquiree Company

Another important aspect in Mergers and Acquisition is the taxability on the Shareholders of the Acquiree Company on the disposal of its shares held in the Acquiree Company. Income Tax Act of Nepal does not have a clear provision as to how the Shareholders of the Acquiree Company will be taxed. In that case, Shareholders of Acquiree Company are left with two alternatives.

Alternative I: As per provision of Section 46(3) read with Rule 16 (1) of Income Tax Rules, "In cases where, by virtue of the unification or restructuring of any entity, the interest of any person in any entity is replaced by another interest of that entity or by the interest of any other entity, an involuntary disposal shall be deemed to have been created." Rule 16(2) provides that "In cases where an involuntary disposal is created pursuant to Sub-rule (1), the entity or person shall submit an application to the Department for an approval" and as per Sub rule (3) The Department may provide approval on the application submitted pursuant to Sub-rule (2).

And in case of involuntary disposal, by virtue of Section 46(1) and 46(2), for the purpose of calculation of gain from disposal of such assets the incoming and net expenses will be equal. Hence the tax base for calculating the tax on such disposal will be nil.

To get the benefit of Section 46, the Tax payer shall submit the application to Inland Revenue Department and it will be applicable, if such application is approved. Now, if the Shareholder of Acquiree Company could not get approval from IRD to invoke Section 46, then there is no clarity as to which section applies.

Alternative II: The Author believes that in case approval from IRD under section 46(3) rule 16 is not available or in general case of merger, taxability to the shareholders of the Acquiree Company can be addressed through Section 47 of Income Tax Act of Nepal "Disposal upon amalgamation of property and liability". As per Section 47 of Income Tax Act, If, as a result of acquisition of any property or bearing of any liability by any person, any other property under ownership of, or any other liability borne by, that person ceases or is amalgamated and thus disposal takes places, then the following provisions shall apply:-

(a) Where net expenses were incurred for the amalgamated property or liability immediately before disposal, that person:

1. Shall be deemed to have received an amount equal to the net expenses in respect of the disposal of the amalgamated property or liability, provided that, such amount shall not exceed the amount received by that person for the amalgamated liability.

2. Shall be deemed to have incurred expenses in a sum equal to that amount in holding ownership or bearing liability of the amalgamated property.

(b) Where net incomes were earned for the amalgamated liability in respect of the amalgamated liability, immediately before the disposal of the liability, that person:

1. Shall be deemed to have incurred expenses in a sum equal to net incomes for the disposal of the amalgamated liability, provided that, in the case of the amalgamated property, that amount shall not exceed the amount spent by that person in acquiring that property.

2. Shall be deemed to have received an amount equal to that amount in holding ownership of or bearing liability of the amalgamated property.

Hence, there will be any tax effect on the Shareholder of the Acquiree Company as the Net Expenses incurred by him will be both Incoming and Outgoing for the purpose of calculating the gain on disposal of his shares.
Taxability to the Merged/Acquirer Company

From the Acquirers perspective, there are two important aspects to be considered while doing mergers and acquisition transaction. First being the Cost base of Assets and Liabilities being transferred to the Acquirer Company from the Acquiree Company and second being the Tax benefits being provided to the Acquirer Company.

Cost base of Assets and Liabilities of Acquiree Company being transferred to the Acquirer Company will depend upon the Value at which such Assets and Liabilities are transferred. If we assume that such Assets and Liabilities are disposed off at Market Value than the Market Value would be the Cost base to the Acquirer Company. But such Assets and Liabilities will be booked at Book Value in the Books of Acquirer Company, if we believe the premise that Section 47 is applicable and such Assets and Liabilities are transferred at Book Value.

Further Section 57 of the Income Tax Act is attracted if the Merger changes more than 50 percent shareholding of the company within a block of 3 Year. As per Section 57(1) of Income Tax Act, "If the ownership of any entity changes by Fifty per cent or more as compared to its ownership until before the last three years, the entity shall be deemed to have disposed the property under its ownership or the liability borne by it." And by virtue of Section 40(3)(E) and Section 41, All the Assets and Liabilities of the Acquirer Company will deem to have been disposed off at the Market Value. Thereby Tax on Disposal of Assets and Liabilities has to be paid on the difference between the Market Value and the Book Value of the Assets and Liabilities.

Further Section 57(2) provides that where more than 50 percent shareholding is changed, following will be the implications for the Acquirer Company:

- The unabsorbed portion of interest carried from previous period as per Section 14(3) is not allowed to set off.
- Losses Carried Forward from previous Years as per Section 20 will not be allowed to set off and carry forward to further years.
- Any adjustment as provided by sec. 25(1) for an amount derived on an accrual basis, the person later disclaims an entitlement to receive the amount or, in the case where the amount constitutes a debt claim of the person, the person write-off the debt as bad, is also not allowed in case it occurs after the change in ownership.
- To subtract, pursuant to Section 36, the loss suffered in disposing any property or liability prior to the change in ownership from the income earned from the disposal of the property or liability after the change in ownership is now allowed.
- In case where the entity accounted for a premium in terms of section 60(2)(b)(1) prior to the change and the entity after that change returns the premium to the insured, such premium is not allowed as expense.
- Carry forward of foreign income tax under section 71(3) that is paid with respect to foreign income prior to the change is also not allowed

Further as per Section 57(3), In cases where the ownership of any entity changes in any manner mentioned in Section 57(1) in any income year, the parts before and after the change in ownership in that income year shall be treated as separate income years. And income tax returns for such separate periods needs to be submitted.

B. Special Provision in case of Mergers and Acquisition of Entities doing Banking and Finance Business or Insurance Business

Income Tax Act of Nepal has formally acknowledged the importance of Tax Benefit in the Mergers and Acquisition with the Finance Bill 2067 that too only for the Entities carrying on Banking and Finance Business or Insurance business by inserting Section 47A.
As per the Section 47A of Income Tax Act- "If entities of similar nature carrying on banking and financial business or insurance business are merged to each other, provisions of Clauses (a), (b), (d), (e), (f) and (g) of Sub-section (2) of Section 57 and Sub-section (3) thereof shall not apply."

Provided that, if there is any loss that could not be deducted of any entity that ceased to exist upon merger, such loss has to be deducted in the coming Seven years on pro rata basis. If the entity that so deducts loss by equal installments is again divided prior to the deduction of loss wholly, tax on the amount deducted for the deducted loss has to be paid at the rate of tax prevailing in the financial year of merger or acquisition.

**Taxability to the Acquiree Company**

In the case of merger of entities doing banking or insurance Business, Income Tax Act vide Section 47A(2) has prescribed manner in which the Assets and Liabilities of Acquiree Company shall disposed off. It provides that If the disposal of assets and liability is made upon the merger of entities pursuant to Sub-section (1), the following shall apply:

(a) In the case of disposal of trade-in-stock and business property:

   (1) The amount equal to the net expenses incurred in that property immediately before the disposal shall be deemed to have been acquired by that person in consideration for that disposal, and

   (2) The amount equal to that set forth in Clause (1) shall be deemed to be the cost incurred by the person acquiring the property.

(b) In the case of disposal of depreciable property:

   (1) The amount equal to the remaining value of the diminishing system of the group pursuant to Section 4 of Schedule-2 at the time of disposal shall be deemed to have been acquired in consideration for that disposal, and

   (2) The amount equal to that set forth in Clause (1) shall be deemed to be the cost incurred by the person acquiring the property.

(c) In the case of disposal of liability:

   (1) The amount equal to that amount whichever is lesser of the market value of the liability and the net income immediately before the disposal shall be deemed to be the cost incurred by that person in consideration for disposal.

   (2) The amount equal to that set forth in Clause (1) shall be deemed to be the cost incurred by the person bearing liability in consideration having borne that liability.

(d) In calculating the cost of merged assets and liabilities, the entity merging business or the entity merged shall calculate only the cost in consideration for assets and liability existed at the time of operation of the merged business by the merged entity (prior to merger or acquisition), pursuant to Clauses (a), (b) and (c).

In case of merger of entities doing banking or insurance business, Section 47A clearly provided that the Assets of Liabilities of Acquiree Company will be disposed off at Book Value and hence there will not any tax liability on such disposal.

**Other Benefits provided**

Section 47A has provided following other benefits for the mergers of entities doing banking or insurance business.

- As per Section 47A(3) Tax deduction shall be made on the payment by giving Fifty percent rebate on the rate of tax deduction to be applied on the retirement pension on the additional lump sum payment (except the payment made through
the retirement fund or the payment to be made as mentioned in the terms and conditions of employees for the purposes of awarding group retirement to the employees serving in the entity disposed upon merger or the entity following merger).

- As per Section 47A(4) The shareholders existing in the entity disposed upon merger pursuant to Section 47A(1) dispose their shares by sale within Two years after the merger, no capital gain tax shall be charged on the profits made on the shares so disposed.

- Further Section 47A(5) provides that Tax shall not be levied on the dividends distributed by the entity that has been disposed upon being merged to the shareholders existing at the time of merger within Two years after the date of merger.

However, to get the benefits of Section 47A the entity that intends to be disposed upon being merger shall give a letter of intent to be merged to the Inland Revenue Department within the time prescribed under section 47A(6) and it shall complete such merger within the time prescribed by Section 47A(7).

C. Issues to be noted

From the above provisions of the Income Tax Act, we understand that the Income Tax Act is not very clear with respect to the Taxability of assets and liabilities and the Quantification of gain/loss from the disposal of assets and liabilities of Acquiree Company not being entity doing banking or insurance business. Further in both the cases whether it is the entity doing banking or insurance business or otherwise, taxability on the disposal of shares of shareholder of Acquiree Company is also not very clear.

Similarly, Taxability on the Disposal of Assets and Liabilities as per Section 57 is something which is very detrimental to the promotion of mergers and acquisition transaction in Nepal. There are two reasons behind this first being by virtue of Section 41(1), Disposal of Assets and Liabilities under Section 57 will be taxed at Market Value less Book Value of Assets/Liabilities, second it will be taxed to the Company not shareholders. This way tax will be levied to both shareholders on the gain on disposal of their shares and to the company for its deemed disposal under Section 57. Taxing Shareholder could be logical, however taxing company under Section 57 where there is no real benefit to the company is not very logical. Section 57 of Income Tax Act of Nepal is similar to the Income Tax Provisions of other South Asia countries for disallowing carry forward of losses in case of change in control. The real intent of Section 57 is just to stop the tax payers to take benefit of carry forward of loss by unreasonable means but not to tax the company in which such change of control happens. More importantly its implication is really huge as it applies even in case of inviting introduction of new shareholders, venture capital firms or even in case of increase in share capital.

D. The Way Forward

With the Globalization, Multinational Companies are dominating every part of the world, and to stay in the ring Domestic Companies need to grow. Hence, it is very important to promote mergers by the government to promote the Domestic Companies to compete with global firms. With the current tax legislations on the Mergers and Acquisitions, it would be very difficult for us to see any Mergers and Acquisitions happening in the Industries other than Banking and Insurance in future. Among other tax reforms required, Nepal needs a better Capital Gain Regime to promote both the Mergers/Acquisition and Foreign Investments. Government need to take a call in this.
TAXATION

Corporate Tax Planning through Use of Losses

Tax planning may be defined as an arrangement of one's financial affairs to take full advantage of all eligible tax exemptions, deductions, concessions, rebates, allowances permitted under the Income Tax Act so that the tax burden is minimized in the hands of the taxpayer without violating the legal provisions.

Ms. Anupama Ghimire

Ms. Ghimire is a CAP III Level student of ICAN. She can be reached at anupama.apg@gmail.com

Tax Planning

Tax incidence can be reduced through tax planning, tax avoidance or tax evasion. Planning is different from avoidance or evasion.

Tax planning may be defined as an arrangement of one's financial affairs to take full advantage of all eligible tax exemptions, deductions, concessions, rebates, allowances permitted under the Income Tax Act so that the tax burden is minimized in the hands of the taxpayer without violating the legal provisions.

Tax avoidance is reducing or negating tax liability in legally permissible ways by structuring one's affairs. Any such transaction would be valid only if it has commercial substance and is not a colorable device.

Tax evasion is the method or means by which the tax is illegally avoided through unacceptable means. It refers to a situation where a person tries to reduce his tax liability by deliberately suppressing the income or by inflating the expenditure, recording fictitious transactions, etc. It's an illegal arrangement where tax liability is hidden.

Tax Losses

Simply put, loss is the excess of deductions over inclusions. You generally make a tax loss when the total deductions you can claim for an income year exceed your income for the year.

Tax losses can be of two types:
- Overall losses (deductions less inclusions)
• Deductions which reduce taxpayers’ profits without necessarily resulting in overall losses

In an ideal tax system, losses of one income year can be carried over to set off with profits of other income years for consistency with the principles of taxable capacity and neutrality of tax systems. However, in practice, for a variety of administrative and budgetary reasons, most tax systems place limitations on utilization of losses for tax purpose. Tax laws or policies are designed to allow, deny or restrict the use of tax losses for tax purpose.

**Carry Back Rules**

When a loss carry-back is allowed, a company offsets losses against preceding years’ income. This retroactively reduces the taxpayer’s tax liabilities related to that previous year and may generate a refund of taxes previously paid.

Arguments in favor of carry-back rules generally are based on the desire to ensure tax neutrality, the net taxation principle, and the implicit support for riskier ventures. If at the time the investment decision is taken, it is known that future losses can be used over time, this may have positive impact on decision makers.

Considerations against the introduction of carry-back rules may be related to governments’ administrative and budgetary concerns. A loss carry-back requires reopening a taxpayer’s assessment or tax return for prior tax periods. Moreover, from a purely fiscal perspective, it creates difficulties in terms of government budgets, if in a tax year, a number of claims are raised for the refund of taxes previously paid.

Based on these reasons, countries may either deny carry-back or may apply time limits to carry-back. Generally in practice, carry back is restricted in tax world.

In Nepal, Section 20(4) of Income Tax Act, 2058 places restriction on carry back of tax losses by the entities except in case of long term contract arranged through International Competitive Bidding. If any person has obtained a long term contract through International Competitive Bidding procedure and has incurred loss upon completion or disposal of contract in an income year or has carried forward loss related to the contract, the person can set off/carry back loss in previous income year/s and the amount of set off/carry back should be limited to the excess of inclusions under the contract in such income year over the deductions.

In Singapore, companies may carry-back unutilized capital allowances (CAs) and trade losses arising in a Year of Assessment (YA) to reduce the amount of taxes payable in an immediately preceding YA. To help small businesses cope with cash-flow problems especially in cyclical downturns, a one-year carry-back of current year unutilized CAs and trade losses was introduced effective from YA 2006.

**Sideways Loss Relief**

A number of countries have so called Scheduler systems of taxation, according to which incomes and gains are divided into different categories based on their source. In most of these countries, losses can be offset only against income from same source, thus preventing sideways loss relief.

In Nepal, any person can set off losses from business or investment in any income year in following manner:

- Loss from other business of such person to the extent not set off by income from that business can be set off with gains from other business and investments of that person.
- While computing income from investment, any person can set off the loss from other investments during that year.
- Loss from foreign country can be set off with income from that particular country only and loss incurred during earning tax exempt income can be set off while calculating exempt income only.
Carry Forward Rules

Unlike carry-back rules, which are adopted by only a few states, loss carry forward rules are present in the vast majority of tax systems because loss carry-forward rules have a more limited impact on a government’s budget and are easier to administer. In several countries, time limitations are introduced in respect of carry forwards. Reason advanced in support of such limitations include the need to prevent abuses, and for practical and administrative considerations.

In Nepal, loss from business can be carried forward up to 7 income years. In case of BOOT made of public infrastructures, hydropower sector and petroleum production, loss can be carried forward for 12 years.

In tax regimes like UK, Sweden, Germany, France, Denmark, Australia and New Zealand, tax losses can be carried forward to indefinite period, while the carry-forward duration is 20 years in countries like US and Canada.

Deductions which Reduce Taxpayers’ Profits

Some tax regimes allow previous years’ losses to set off with capital gains or to increase capital loss of an income year.

Section 36 of Income Tax Act, 2058 of Nepal allows net loss from business of previous years and any unrelieved losses due to lapse of set off period (i.e. 7 years and 12 years) to be set off with gains from disposal of business assets and business liabilities. This provision reduces the capital gains to be included in income for that particular income year. If there is net loss after set off of such losses, such net loss is carried forward to be set off with gains on disposal of Business Assets/Business Liability in future periods.

Restrictions

Loss carry over (forward and backwards) rules are, in most states, subject to further restrictions, generally related to the change of ownership or activity of the entity claiming the loss relief. These restrictions are aimed at ensuring that the loss relief is granted exclusively to the person that economically incurred such losses and at counteracting aggressive tax planning schemes on losses.

In Nepal, in case there is change in control of ownership under Section 57 of Income Tax Act, 2058, the losses including the following tax attributes incurring prior to such change cannot be set off with profits after such change.

- If the entity whose control of ownership has been changed is the resident entity controlled by tax exempt entity as defined by Section 14 and has paid interest to such controlling entity and the amount of such interest exceeds the limit prescribed by Section 14 (2), and hence can be set off as per Section 14 (3), then amount cannot be set off after change in such control.

- Loss incurred prior to change in control of ownership cannot be carried forward to the period after such change as per Section 20. Even if the loss was caused due to the change in such control, such cannot be carried forward.

- Losses incurred after such change in control cannot be carried back to set off with earlier years as per Section 20 (4).

- If the amount booked as income or expense on accrual basis prior to change in ownership is received or paid later after such change and there is a difference between such amounts due to change in exchange rates, then such difference cannot be set off as per Section 24.

In addition, general and specific anti-avoidance rules are often used to deny benefits to tax payers in relation to aggressive tax planning schemes on losses.
Tax Planning Schemes

In 2011, OECD Secretariat conducted study of immediate tax revenue impact due to losses from global economic and financial crisis, and result of the normal operation of countries’ loss relief rules if companies turn to aggressive tax planning.

The report of the study reflects the experiences of 17 countries who participated in the study team: Australia, Austria, Canada, Denmark, France, Germany, Ireland, Italy, Mexico, Netherlands, New Zealand, Norway, Spain, Sweden, Switzerland, UK and US, where aggressive tax planning involving corporate losses was observed. The report summarizes aggressive tax planning schemes encountered by revenue authorities in participating countries, together with their detection and response strategies.

The report identified three key risk areas in relation to the use of losses for tax purpose which are use of financial instruments, corporate reorganizations and non-arm’s length transfer pricing. Based on the intended result, schemes encountered by participating countries were divided into following categories:

1. Loss shifting schemes
2. Schemes shifting profits to a loss making party
3. Schemes circumventing time restrictions on the carry-over of losses
4. Schemes circumventing change of ownership/activity restrictions on the carry-over of losses
5. Schemes circumventing rules on the recognition or treatment of losses
6. Schemes creating artificial losses and
7. Schemes involving dual/multiple use of the same loss.

Few Examples

An example is acquisition of loss making entity by a profit making entity with the intention of utilization of unused tax losses of that entity. In Nepal, banks and insurance companies can take benefit of loss utilization through such corporate restructuring schemes. However for other businesses, Section 57 of Income Tax Act 2002 restricts the carry forward of unused tax losses in the event of change in ownership.

In such cases, injection of income into a loss making company immediately prior to ownership change would result in full utilization of unused losses. Income can be injected in the form of grants, sale of stock, transfer from unearned income, reduced depreciation charges in newly acquired Pool E assets, etc. However, it is necessary to establish the arm’s length consideration to avail the benefit. Also, as per Section 57, the assets and liabilities of the entity are deemed to be disposed at market value, which may generate taxable profit to be set off with existing tax losses.

Another example is of a resident parent company with taxable profits having several subsidiaries and act as distributors and have incurred large operating losses. Parent company makes large payments to subsidiaries as market support payment and claims these payments as deductions, shifting the losses of subsidiary to the parent company.

There can be observed many other instances of tax planning through use of losses. It should be noted that the Inland Revenue Department has the authority to re-characterize or disregard an arrangement or part of an arrangement that is entered into or carried out as part of a tax avoidance scheme, which are termed as general anti-avoidance rule (GAAR) as well as Specific anti-avoidance rule (SAAR). Also, the interpretations of certain provisions may be changed through rulings and circulars.
**Activities**

**Workshop on Anti-Money Laundering**

The Contemporary Issue Discussion Committee of the Institute organized half day workshop on Anti-Money laundering on April 22, 2016 in Kathmandu.

CA. Sunil Jakibanja the Chairperson of Contemporary Issue Discussion Committee is welcoming the participants.

CA. Sunil Jakibanja the Chairperson of Contemporary Issue Discussion Committee welcomed the participants and highlighted the objectives of the program. This program was conducted in two sessions.

<table>
<thead>
<tr>
<th>Session</th>
<th>Topics</th>
<th>Paper Presenter</th>
</tr>
</thead>
<tbody>
<tr>
<td>Session 1</td>
<td>History of Anti-money Laundering: An Overview</td>
<td>CA. Maha Prasad Adhikari, Former Deputy Governor, Nepal Rastra Bank</td>
</tr>
<tr>
<td>Session 2</td>
<td>Anti-Money laundering/Combating the Financing of Terrorism(AML/CFT)</td>
<td>CA. Devendra Gautam, Certified Anti Money Laundering Specialist</td>
</tr>
</tbody>
</table>

In the program the former Deputy Governor of Nepal Rastra Bank CA. Maha Prasad Adhikari and Certified Anti Money Laundering Specialist CA. Devendra Gautam presented the papers. 5 CPE Credit hours was granted to member of ICAN who participated in the program. Altogether 98 individuals attended the workshop.

**Interaction Program**

Anti-Money Laundering Department organized an interaction program on ”Role of Non-financial Professionals on Anti-Money Laundering” in association with Institute of Chartered Accountants of Nepal on 9 May 2016.

CA. Prakash Lamsal, President speaking on the program.

The professionals highlighted the role of auditor in effective implementation of Anti-Money Laundering Act (AMLA) in the program. In the forum, AMLD requested the auditors to remain cautious while rendering the audit services and comply with the provision of the Act that require some reporting on suspicious transactions to Financial Information Unit (FIU).
Conference on “Emerging Issues in Accounting Profession”

The Institute of Chartered Accountants of Nepal (ICAN) organized a Conference on “Emerging Issues in Accounting Profession” on 27 May, 2016 (Jestha 14, 2073), Friday at Soaltee Crowne Plaza, Kathmandu.

The Program was formally inaugurated by the ICAN President CA. Prakash Lamsal with inaugural speech.

This Conference was focused on emergence and drivers for Cloud Computing, technical and outsourcing challenges from Business/Client perspective preparing auditors in areas of cloud - governance, risk and Assurance frameworks based on Global standards and frameworks, as well as other contemporary Issues in Accounting Profession including Forensic Audit. In the Conference, the topic namely ethical requirements on marketing & publicity of professional accountants and networking of the firms were presented and discussed their components.

<table>
<thead>
<tr>
<th>Session</th>
<th>Topics</th>
<th>Paper Presenter</th>
<th>Chairperson</th>
<th>Commentator</th>
</tr>
</thead>
<tbody>
<tr>
<td>Session 2</td>
<td>Cloud Computing: To cloud or not to cloud?</td>
<td>Mr. Vivek Rana, ISO 27001 LA, CISA</td>
<td>CA. Sanir Kumar Dhungel, Chairman, Auditing Standard Board and Past President, ICAN</td>
<td>Prof. Dr. Subarna Shakya, DECE, Pulchowk Campus, T.U.</td>
</tr>
<tr>
<td>Session 3</td>
<td>Forensic Audit- Relevant in Present Scenario</td>
<td>CA. Nanda Kishor Sharma, Past Chairman of Auditing Standards Board</td>
<td>CA. Pradeep Kumar Shrestha, Past President, ICAN</td>
<td>CA. Mahesh Kumar Guragain, Past President, ICAN</td>
</tr>
</tbody>
</table>

ICAN Vice-President CA. Mahesh Khanal concluded the program with his closing remarks. Altogether 90 individuals including members and non-members participated in the conference.

The ICAN members who participated in the conference were awarded 8 (eight) CPE credit hours.
Training Course on NAS/NFRS

RA. Member Capacity Development Committee of the Institute successfully conducted training courses on NAS/NFRS at Chitwan, Nepalgunj, Pokhara and Itahari on April 7-9, May 6-8, June 10-12, and June 24-26, 2016 respectively. Following are the details of trainings held in those locations.

<table>
<thead>
<tr>
<th>Date</th>
<th>Topics</th>
<th>Place</th>
<th>Trainer</th>
<th>No of Participants</th>
</tr>
</thead>
<tbody>
<tr>
<td>April 7-9, 2016</td>
<td>Conceptual framework, Presentation of Financial Statements (NAS 1)</td>
<td>Chitwan</td>
<td>CA. Mukunda Dev Adhikari, CA. Bishnu Prasad Bhandari</td>
<td>29</td>
</tr>
<tr>
<td></td>
<td>Inventories (NAS 2) and Property, Plant and Equipment (NAS 16),</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Provisions, Contingent Liabilities and Contingent Assets (NAS 27),</td>
<td>Nepalgunj</td>
<td>CA. Mukunda Dev Adhikari, CA. Bishnu Prasad Bhandari</td>
<td>27</td>
</tr>
<tr>
<td></td>
<td>Accounting Policies, Changes in Accounting Estimates &amp; Error (NAS 8),</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Revenue (NAS 18), Borrowing Cost (NAS 23),</td>
<td>Pokhara</td>
<td>CA. Suresh Devkota, CA. Bishnu Prasad Bhandari</td>
<td>24</td>
</tr>
<tr>
<td>June 10-12, 2016</td>
<td>Events after the Reporting Period (NAS 10), Agriculture (NAS 45),</td>
<td>Itahari</td>
<td>CA. Mukunda Dev Adhikari, CA. Bishnu Prasad Bhandari</td>
<td>33</td>
</tr>
<tr>
<td></td>
<td>Income Taxes (NAS 12), Construction Contract (NAS 32),</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Statement of Cash flow (NAS 7)</td>
<td></td>
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</tbody>
</table>

The Institute conducted NAS/NFRS Training with the objective of enhancing knowledge and understanding on NFRS/ NAS of the participants. The training courses were delivered by the eminent expert of the related field.

**Representation on Workshop**

The World Bank organized a workshop on the Report on Observance of Standards and Codes- Accounting and Auditing (ROSC- AA) in Kathmandu on 22 June 2016. The ICAN representatives participated in the program. The program was chaired by Coordinator, PEFA Secretariat Mr. Kewal Bhandari and President CA. Prakash Lamsal Co-chaired the program. Mr. Rajendra Prasad Nepal, Financial Comptroller General of Nepal was Chief Guest of the Program. The Country Manager of the World Bank Mr. Takuya Kamata delivered welcome speech and Financial Management Specialist of the World Bank Mr. Yogesh Bom presented ROSC Report by highlighting the Key findings in the program. Program Manager of the World Bank Mr. Franck Bessette, President CA. Prakash Lamsal and the Chief Guest of the Program Mr. Rajendra Prasad Nepal offered their remarks on the program. Speaking on the occasion CA. Prakash Lamsal underlined the current scenario of the Institute and the obligations that need to be fulfilled in accordance with the IFAC framework that include the obligation of Quality Assurance, pronouncement of Code of Ethics, Chartered Accountancy curriculum in line with IES, investigative and disciplinary system for its members, mandatory CPE for its members and so on. The representatives of the ICAN comprised of President, CA. Prakash Lamsal, Vice-President CA. Mahesh Khanal, Council Members CA. Prakash Jung Thapa, CA. Bhaskar Singh Lala, RA. Dhurba Paudel, Executive Director CA. Binay Prakash Shrestha and Joint Director, Mr. Binod Neupane. The program was concluded with the closing remarks of the Chairperson.

**Student News**

**Participation in Kantipur HISSAN Edu Fair 2016**

The Institute of Chartered Accountants of Nepal participated in Kantipur HISSAN Edu. Fair 2016 at Brikhuti mandap, Kathmandu from 19-22 May, 2016 jointly organized by Higher Secondary School’s Association Nepal (HISSAN) and Kantipur Publication. During the Fair about 800 students and other stakeholders visited the ICAN stall to get various information with regards to enrollment procedure, fees structure, future career opportunities after completion of the course etc. for pursuing Chartered Accountancy education.

**Chartered Accountancy Career Expo, 2016**

The Institute of Chartered Accountants of Nepal organized two days Career Expo, 2016 in association with five accredited institutions in 14-15 May, 2016 in Kathmandu.
The five accredited institutes were CIMA Academics Pvt. Ltd., CAI Pvt. Ltd., CAI Pvt. Ltd., Elite Institute of Management Pvt. Ltd. and Chaitanya Institute of Management Pvt. Ltd. participated in the career expo, 2016. This expo was organized to promote and disseminate the importance of Chartered Accountancy education to the stakeholders.

During the fair approximately 400 students, parents and other stakeholders visited the ICAN stall and obtained firsthand information about future prospects including career prospects in Nepal on completion of the CA course.

Chartered Accountancy Final Examination

The Institute of Chartered Accountants of Nepal conducted Chartered Accountancy final examination of CAP I, CAP II and CAP III level from 1 to 9 June, 2016. The all levels examination was conducted in Kathmandu and CAP I and CAP II level examination was also conducted at its branches at Pokhara, Biratnagar, and Birgunj. The group wise applicants and appeared numbers in different levels of examinations is as follows.

<table>
<thead>
<tr>
<th>Level</th>
<th>Both Group</th>
<th>Group I</th>
<th>Group II</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>CAP I</td>
<td>Applied</td>
<td>401</td>
<td>-</td>
<td>401</td>
</tr>
<tr>
<td></td>
<td>Appeared</td>
<td>376</td>
<td>-</td>
<td>376</td>
</tr>
<tr>
<td>CAP II</td>
<td>Applied</td>
<td>734</td>
<td>391</td>
<td>1486</td>
</tr>
<tr>
<td></td>
<td>Appeared</td>
<td>695</td>
<td>316</td>
<td>1325</td>
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<tr>
<td>CAP III</td>
<td>Applied</td>
<td>215</td>
<td>182</td>
<td>547</td>
</tr>
<tr>
<td></td>
<td>Appeared</td>
<td>212</td>
<td>168</td>
<td>511</td>
</tr>
<tr>
<td>Total</td>
<td>Applied</td>
<td>1350</td>
<td>573</td>
<td>2434</td>
</tr>
<tr>
<td></td>
<td>Appeared</td>
<td>1283</td>
<td>484</td>
<td>2212</td>
</tr>
</tbody>
</table>

The total applicants in all level of CA examination were 2434 out of which 2212 appeared at least in one subject.

Membership Examination

The Institute of Chartered Accountants of Nepal conducted Chartered Accountancy membership examination of Paper 4 and Paper 6 in June 5 and 7, 2016. As per the Rule 42 of Nepal Chartered Accountants Regulation, 2061 the person holding Chartered Accountant’s qualification from foreign accounting body are required to appear in the membership examination conducted by ICAN for obtaining membership of the Institute. The total applicants for the examination in Corporate Law and Advanced Taxation were 170 and 171 whereas the examinees appeared were 147 and 139 in the respective subjects.

Students Enrollment in Different Levels

The student enrollment status in CAP I, CAP II and CAP III levels of chartered accountancy and accounting technician courses from April to June 2016 is as follows:

<table>
<thead>
<tr>
<th>Level</th>
<th>CAP I</th>
<th>CAP II</th>
<th>CAP III</th>
<th>AT</th>
</tr>
</thead>
<tbody>
<tr>
<td>Number</td>
<td>569</td>
<td>3</td>
<td>9</td>
<td>1</td>
</tr>
</tbody>
</table>
Hall Test for CAP II and CAP III

The Institute of Chartered Accountants of Nepal conducted hall test for CAP II and CAP III level of chartered accountancy course. Hall test is mandatory for all CAP II and CAP III level students for appearing in final examination of respective level. During the period of April to June 2016 the Institute conducted 13 hall tests and a total number of 5792 students appeared in tests in different subject(s).

One year Internship for Foreign CA Qualification Holders

Pursuant to Nepal Chartered Accountants Regulation, 2061, Rules 41 (Ka) (5th amendment), the Institute of Chartered Accountants of Nepal has made mandatory provision of one year internship to the foreign CA qualification holders for getting Membership and Certificate of Practice. During the period of April to June, 2016 a total of 35 Chartered Accountants who qualified from ICAI have joined one year internship in various firms.

Crash Course

The Institute of Chartered Accountants of Nepal conducted 10 days Crash Course to CAP III level students from 14 April to 23 April, 2016. During the course Advance Accounting, Taxation, Auditing and Law subjects were delivered. Altogether 31 students participated in the course.

Career Counseling and Career Seminar

The Institute is using Career Counseling mechanism as an effective tool to attract the new students for studying Chartered Accountancy education. Approximately 200 students in Kathmandu valley and 1000 students in outside the valley actively participated in the counseling program. Similarly, the Institute organized career seminar in Pokhara, Butwal Nepalgunj and Biratnagar focusing the students. Details are as follows:

<table>
<thead>
<tr>
<th>S. No</th>
<th>Location</th>
<th>Date</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Pokhara</td>
<td>2073, Jestha 04</td>
</tr>
<tr>
<td>2</td>
<td>Butwal</td>
<td>2073, Jestha 11</td>
</tr>
<tr>
<td>3</td>
<td>Nepalgunj</td>
<td>2073, Jestha 14</td>
</tr>
<tr>
<td>4</td>
<td>Biratnagar</td>
<td>2073, Ashar 12</td>
</tr>
</tbody>
</table>

Interaction between President, Vice-president and NCASA

On 29 April, 2016 the newly elected member of Nepal Chartered Accountants Student Association (NCASA) met with the President, Vice-president, Council member and Election Committee members at ICAN premises and discussed on students related matters.

Mr. Rishi Ram Pokharel has been elected as President of NCASA. The election was held on 23 April, 2016.

Accounting Technician Examination Results Published

In pursuance of Bye-Law 17 of the Accounting Technician Bye-Laws, 2067, the result of the Accounting Technician Examination held in March 2016 has been published on 12 May, 2016. According to the results Mr. Dipendra Timilsena (AT 00246), Mr. Lil Bahadur Thapa (AT 00248) and Mr. Pappu Kumar Gupta (AT 00288) declared pass in the AT examination. Altogether 12 Students studying Accounting Technician courses appeared in the examination.
Membership, Certificate of Practice and Auditing firm

The status of total number of Membership, Certificate of Practice issued, Audit Firms and renewal status from 17 July, 2015 to 30 June, 2016 (16 Ashad, 2073) is as follows:

<table>
<thead>
<tr>
<th>Category</th>
<th>Membership</th>
<th>COP</th>
<th>Firm</th>
</tr>
</thead>
<tbody>
<tr>
<td>FCA/CA</td>
<td>986</td>
<td>710</td>
<td>721</td>
</tr>
<tr>
<td>RA-B</td>
<td>3380</td>
<td>1960</td>
<td>3145</td>
</tr>
<tr>
<td>RA-C</td>
<td>1603</td>
<td>864</td>
<td>1471</td>
</tr>
<tr>
<td>RA-D</td>
<td>2284</td>
<td>1276</td>
<td>2092</td>
</tr>
<tr>
<td>Total</td>
<td>8253</td>
<td>4810</td>
<td>7429</td>
</tr>
</tbody>
</table>

Registration of New Chartered Accountant

During the period of 1 April, 2016 to 30 June, 2016 the Institute of Chartered Accountants of Nepal has given membership to 39 new Chartered Accountant pursuant to Section 16(2) of Nepal Chartered Accountant Act, 1997. The List of new Chartered Accountant Members registered is as follows:

<table>
<thead>
<tr>
<th>S. No.</th>
<th>Mem. No.</th>
<th>Name</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>949</td>
<td>KRIPA SHRESTHA</td>
</tr>
<tr>
<td>2</td>
<td>950</td>
<td>SUJIT POKHAREL</td>
</tr>
<tr>
<td>3</td>
<td>952</td>
<td>PRACHAND DHOJ KARKI</td>
</tr>
<tr>
<td>4</td>
<td>953</td>
<td>NISHAN POUDEL</td>
</tr>
<tr>
<td>5</td>
<td>954</td>
<td>SHAILESH DALLAKOTI</td>
</tr>
<tr>
<td>6</td>
<td>956</td>
<td>RISHI KESH PAHARI</td>
</tr>
<tr>
<td>7</td>
<td>958</td>
<td>RISHI RAM CHALISE</td>
</tr>
<tr>
<td>8</td>
<td>959</td>
<td>SURESH SHARMA</td>
</tr>
<tr>
<td>9</td>
<td>960</td>
<td>BALARAM PARAJULI</td>
</tr>
<tr>
<td>10</td>
<td>961</td>
<td>MURALI DHAR JOSHI</td>
</tr>
<tr>
<td>11</td>
<td>962</td>
<td>NABINA THAPA</td>
</tr>
</tbody>
</table>

File Upgrading Result Published and Written Examination Conducted

In accordance with Section 30 (Kha) of Nepal Chartered Accountants Act, 2053 and Rule 54 (2) and (3) of Nepal Chartered Accountants Regulation 2061, the result of the class upgrading of COP has been published on 19 April, 2016. According to the results 5 RA “C” class members were upgraded to “B” class and 1 RA “D” class member upgraded to “C” class. The name of the successful member is as follows:

<table>
<thead>
<tr>
<th>S. No.</th>
<th>Mem. No.</th>
<th>Name</th>
</tr>
</thead>
<tbody>
<tr>
<td>12</td>
<td>963</td>
<td>SHRISTI KHADKA</td>
</tr>
<tr>
<td>13</td>
<td>964</td>
<td>UJJWAL LAMICHHANE</td>
</tr>
<tr>
<td>14</td>
<td>974</td>
<td>RUPESH BHANDARI</td>
</tr>
<tr>
<td>15</td>
<td>965</td>
<td>ANIL LAMICHHANE</td>
</tr>
<tr>
<td>16</td>
<td>966</td>
<td>TRIPTI D.C.</td>
</tr>
<tr>
<td>17</td>
<td>967</td>
<td>LAXMI PAUDEL</td>
</tr>
<tr>
<td>18</td>
<td>968</td>
<td>UDDHAB SILWAL</td>
</tr>
<tr>
<td>19</td>
<td>969</td>
<td>RAJA RAM KADEL</td>
</tr>
<tr>
<td>20</td>
<td>970</td>
<td>ANUJA ADHIKARI</td>
</tr>
<tr>
<td>21</td>
<td>972</td>
<td>NIRAJ SHRESTHA</td>
</tr>
<tr>
<td>22</td>
<td>973</td>
<td>SITARAM WAGLE</td>
</tr>
<tr>
<td>23</td>
<td>975</td>
<td>UTSAV PANTHI</td>
</tr>
<tr>
<td>24</td>
<td>977</td>
<td>KRIPSAN MANANDHAR</td>
</tr>
<tr>
<td>25</td>
<td>979</td>
<td>ANUP KUNWAR CHHETRI</td>
</tr>
<tr>
<td>26</td>
<td>980</td>
<td>MANOJ THAPALIYA</td>
</tr>
<tr>
<td>27</td>
<td>981</td>
<td>YUGADI LUITEL</td>
</tr>
<tr>
<td>28</td>
<td>982</td>
<td>NAMISHA BHATTARAI</td>
</tr>
<tr>
<td>29</td>
<td>983</td>
<td>ISHWAR BHATTARAI</td>
</tr>
<tr>
<td>30</td>
<td>984</td>
<td>NARAHARI ADHIKARI</td>
</tr>
<tr>
<td>31</td>
<td>985</td>
<td>MANOJ KUMAR BHATT</td>
</tr>
<tr>
<td>32</td>
<td>986</td>
<td>SHIVAKUMAR SHAH</td>
</tr>
<tr>
<td>33</td>
<td>989</td>
<td>PRIYANK POKHREL</td>
</tr>
<tr>
<td>34</td>
<td>987</td>
<td>KEDAR NATH BASTOLA</td>
</tr>
<tr>
<td>35</td>
<td>988</td>
<td>PRATISH SHAKYA</td>
</tr>
<tr>
<td>36</td>
<td>990</td>
<td>SUJAN SHRESTHA</td>
</tr>
<tr>
<td>37</td>
<td>991</td>
<td>SUBASH POUDEL</td>
</tr>
<tr>
<td>38</td>
<td>992</td>
<td>NARAYAN BHURTEL</td>
</tr>
<tr>
<td>39</td>
<td>993</td>
<td>HEMLAL BANDARI</td>
</tr>
</tbody>
</table>
Similarly, RA. Prem Prasad Sapkota, membership number 6089 was declared successful in Group I in the upgrading examination. The Institute conducts class upgrading examination every year. The Institute upgrades its member in two ways either by written examination or by evaluation process.

Similarly, Written examination was conducted on 3rd and 5th June, 2016 in Kathmandu. Only one applicant appeared in 2nd group examination to upgrade his membership from C to B Class.

International News

SAFA Board, Committee and SAFA-IFAC Regional PAIB Forum

A four member delegation headed by President, CA. Prakash Lamsal attended SAFA Board, Committee and SAFA-IFAC Regional PAIB Forum held in Mumbai, India from 9-12 April, 2016. The other delegates from ICAN were Council Members CA. Jagannath Upadhyay and RA. Surya Prasad Adhikari and Chairman SAFA Committee / ICAN former President, Dr. CA. Suvod Kimar Karn.

CAPA AGM, CAPA Board Meeting and FRED 2 Conference

A four member team led by President, CA. Prakash Lamsal attended CAPA AGM, CAPA Board Meeting and FRED 2 Conference held in Kuala Lumpur, Malaysia from 16-19 April, 2016. The other delegates from ICAN were Council Members CA. Suresh Devkota, RA. Yadav Prasad Nyaupane and Mr. Mukunda Raj Panthi.

Congratulation to Newly Elected President and Vice-President

CA. Mahesh Khanal is a newly elected President of ICAN. Currently he is serving the Institute as a Vice-president and working in various Committees. He has completed chartered accountancy course from Institute of Chartered Accountants of India (ICAI) in 1997 AD and also completed PG Diploma on MCMIS from Maastricht School of Management, the Netherlands in 1999 AD.

CA. Prakash Jung Thapa is a newly elected Vice-president of ICAN. Currently he is serving the Institute as a Council member and working in different Committees. He has completed chartered accountancy course from Institute of Chartered Accountants of India (ICAI) in 1995 AD and also completed chartered accountancy course from the Institute of Chartered Accountants in Australia (ICAA) in 2009 AD.
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