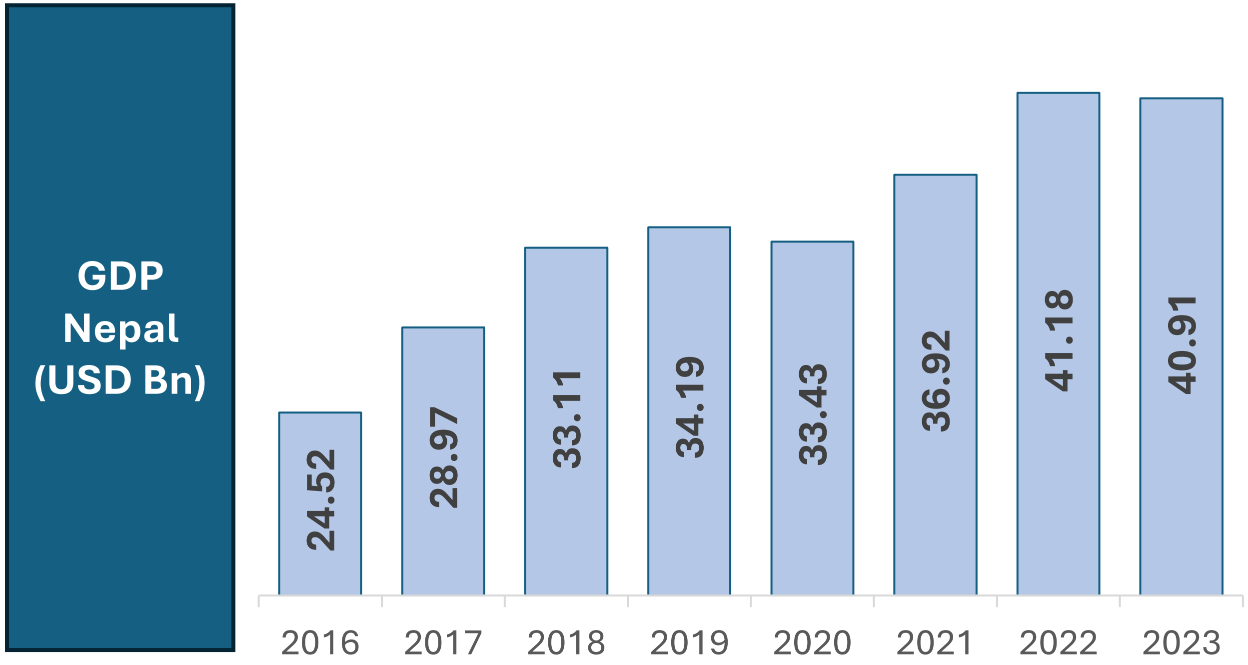
Tax Reform Proposal for Telecom Sector in Nepal

Executive Summary

- While Mobile Telecom sector contributes 1.2% of GDP in Nepal, it pays 3.4% of the taxes (~3X which is higher than even alcohol and tobacco industries).
- Mobile sector pays 60% of revenue as taxes, 31% of which are sector specific to mobile telecom.
- Lower taxes in telecom result in higher Mobile Connectivity Index score (as operators have more funds to invest in quality & coverage of network) which has direct correlation with better GDP per capita. As economy is stimulated, higher tax is earned eventually.
- ICT sector requires backbone of telecom to grow.
- Nepal follows a “revenue maximization through taxation” approach in telecom against other countries like China, Thailand, Bhutan, India, Srilanka with better MCI score. **Taxation without sector discrimination** is recommended in short term.

Telecom sector in Nepal is under stress and contribution to GDP has been continuously declining. But despite 1.2% in GDP contribution in 23/24, Mobile sector contributes 3.4% of revenue collected by govt indicating higher sector specific taxes.



Telecom sector as % of GDP	3.9%	3.4%	3.0%	2.7%	2.4%	2.2%	1.9%	1.8%

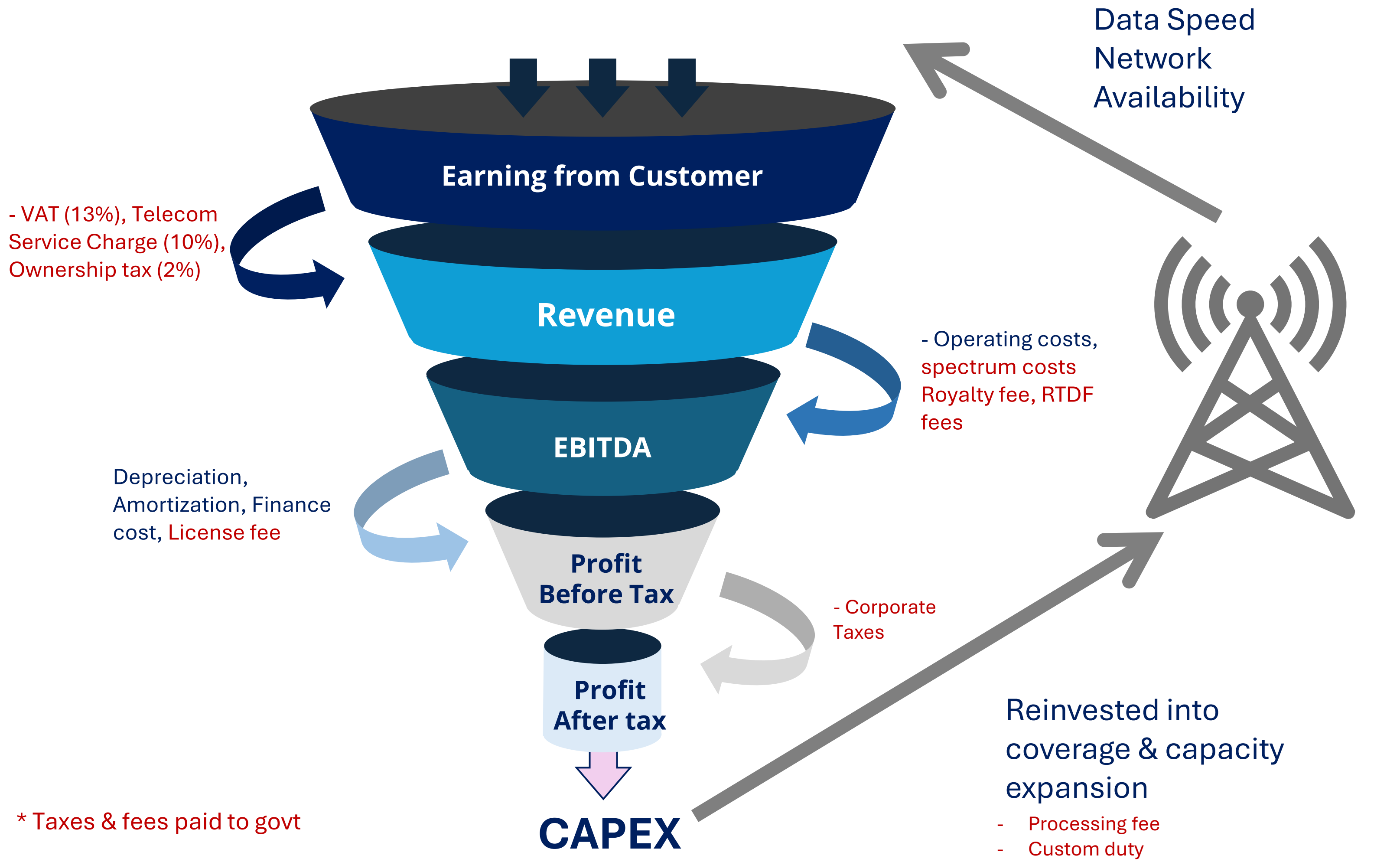
Source:
GDP: World bank
Telecom sector revenue & others : Internal estimates
** NTA (2023)*

	23/24	Bn NPR	Contribution %
Revenue	GDP	5,705	1.2%
	Mobile sector revenue	68.5	
Taxes & Fees	Govt Revenue	1093	3.4%
	Mobile Sector Taxes	37.7	

3X

Tax contribution for Telecom is almost 3X revenue contribution - <u>higher than tobacco and alcohol</u> manufacturing and distribution industry in Nepal.

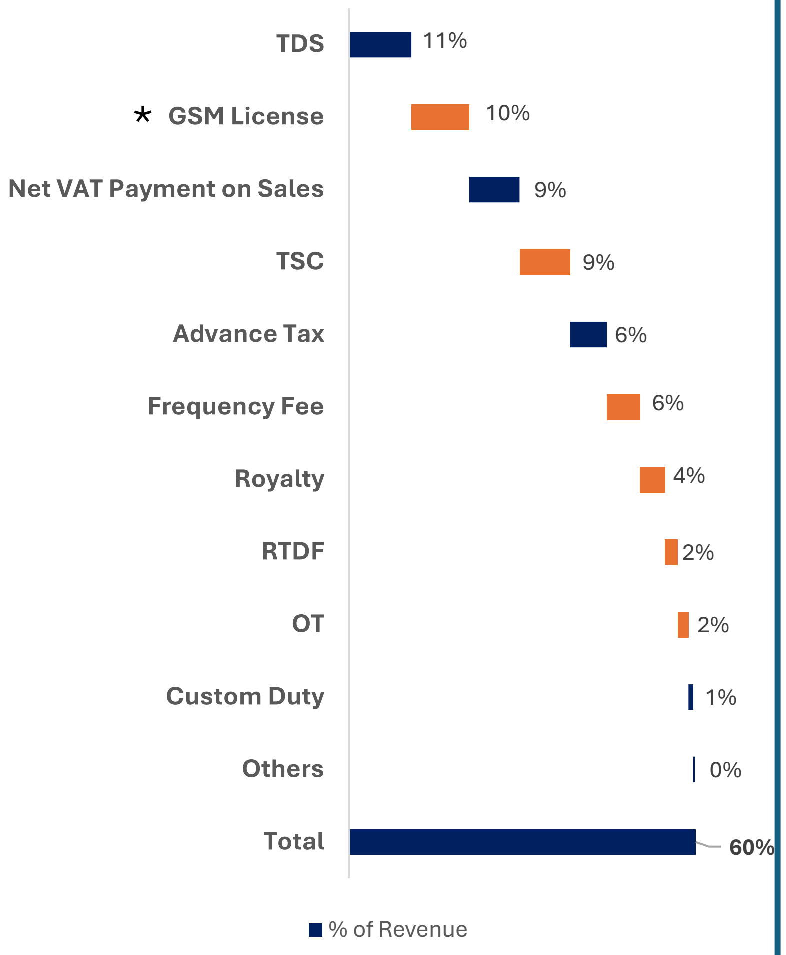
Telecom Companies in Nepal paid 60% of its revenue to the government in the form of taxes and fees, more than half of which are sector specific. Reducing this can allow more investment to flow in the form of CAPEX to improve quality of Telecom Service in Nepal.



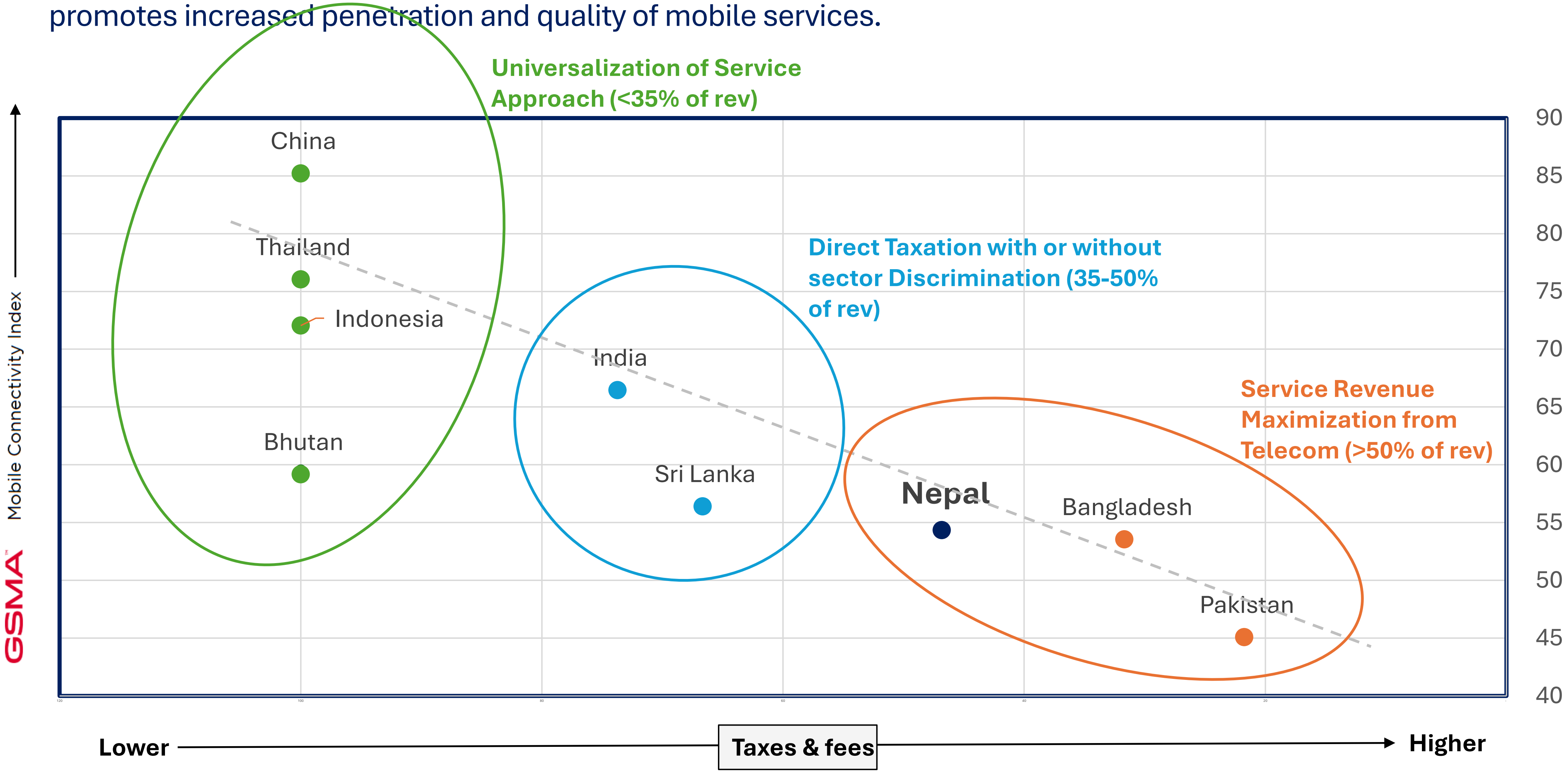
* Taxes & fees paid to govt

Sector Specific taxes/ fees – 31%

Tax & Fees paid to govt as % of revenue on 23/24 by Telecom Companies

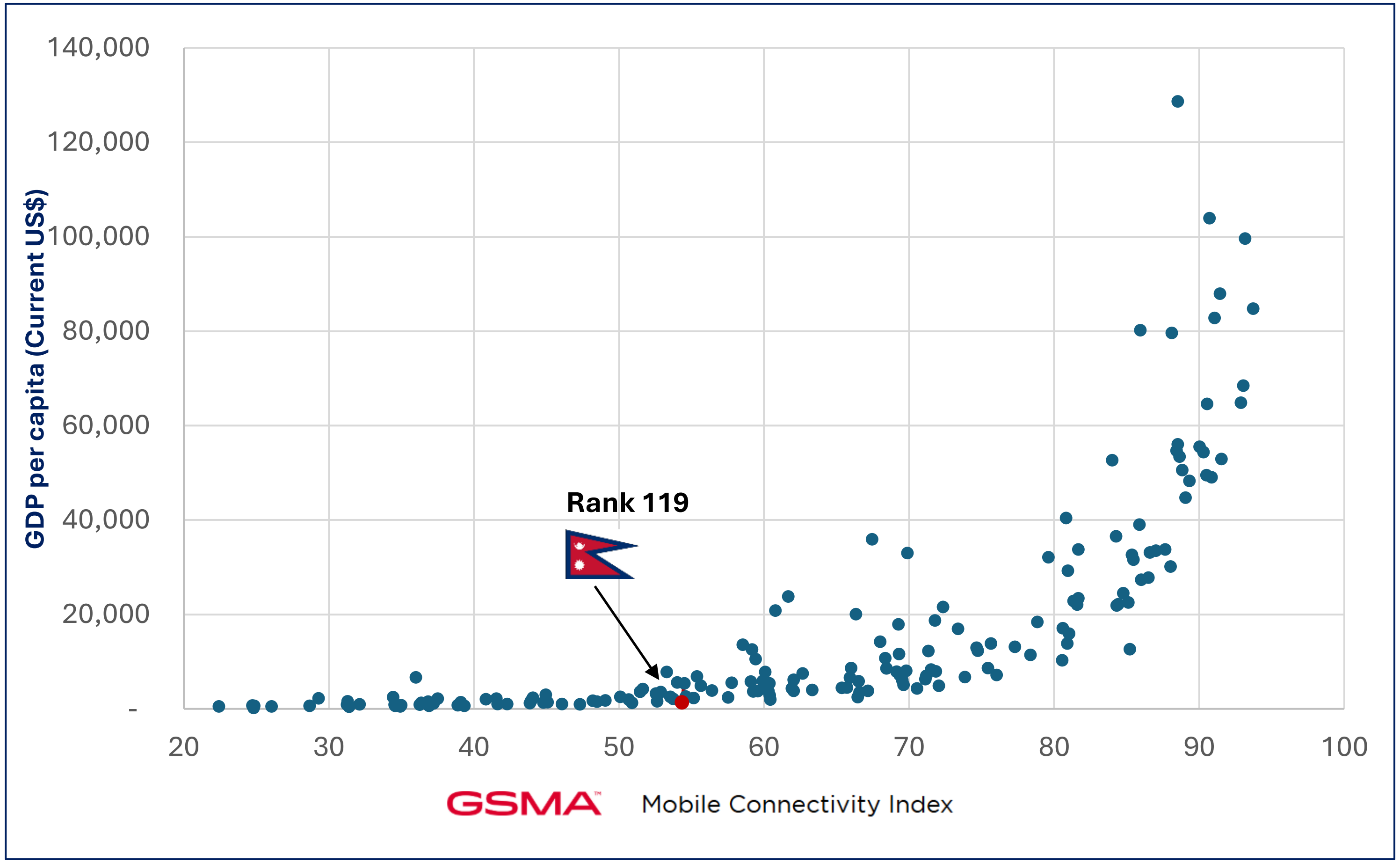


Within the Asia-Pacific region, mobile connectivity is higher in countries where operators make lower tax payments as the operators have more funds to spend on investment in better infrastructure, which in turn promotes increased penetration and quality of mobile services.

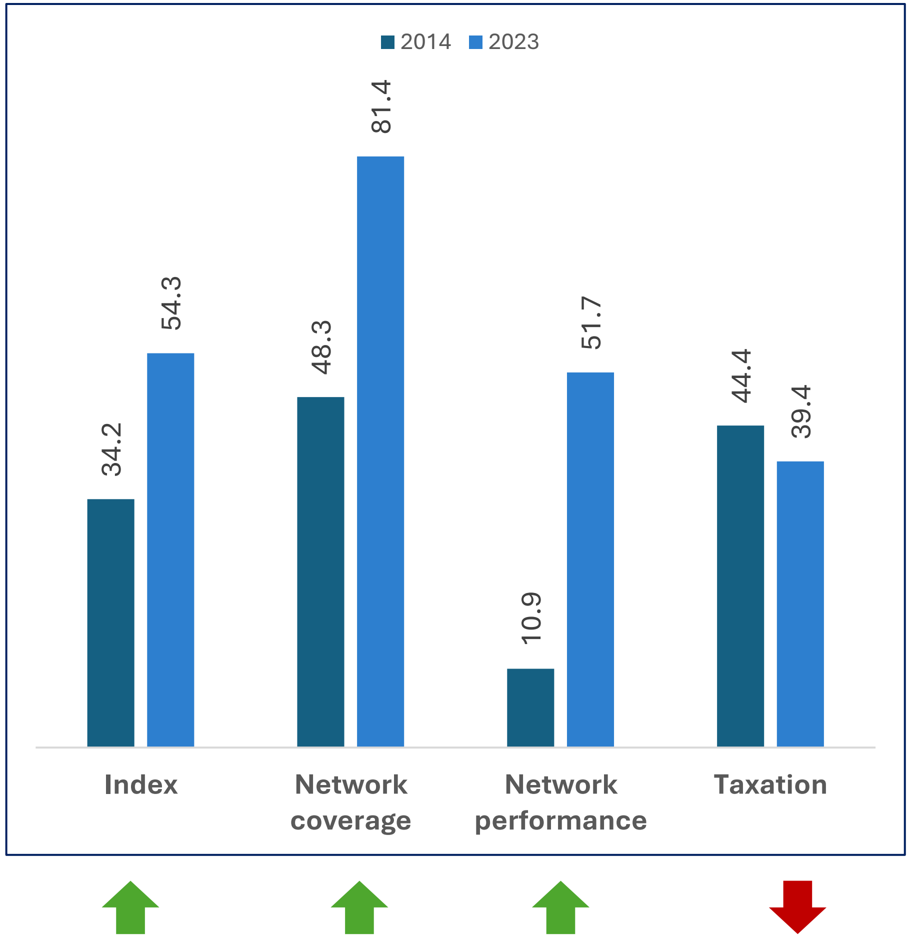


The GSMA Mobile Connectivity Index (MCI) 2023 places Nepal at 119th rank. While MCI enabler dimensions show network coverage and performance have improved considerably over the last decade, Nepal falls behind in favorable regulatory policy scores, esp taxation.

MCI correlation with GDP per Capita



MCI Enabler Dimensions Scores (2023 vs 2014) - Nepal



Source:
Mobile Connectivity Index (GSMA)
GDP per capita 2023 (World bank)

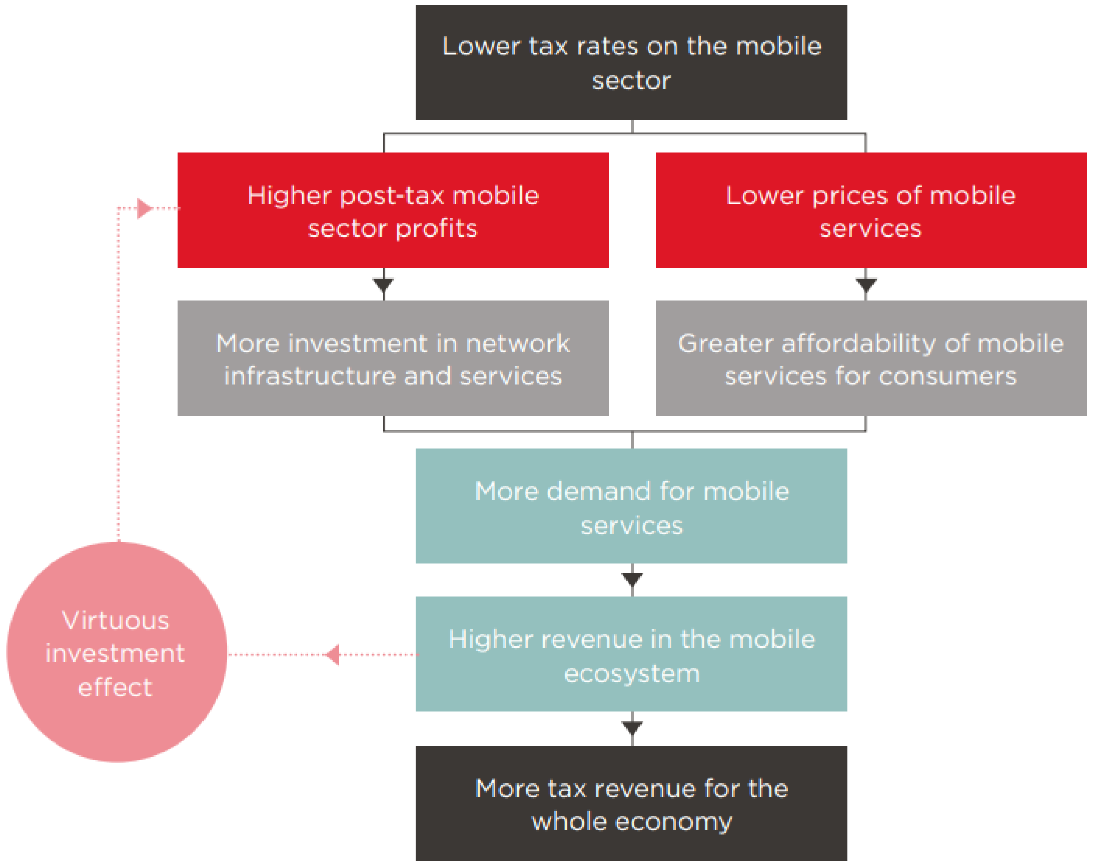
Comparison by Tax Category for Countries in Asia Pacific

Country	VAT/GST	Corporate Tax	License Fee	Tax on Usage	Turnover tax	Other Taxes/Fees	Tax support to Telecom Industry	GSMA taxation score	Category
China	6% VAT	25%. High-tech enterprises encouraged by the state may be eligible for a 15% rate.					Transitioned to an 11% VAT rate for basic telecommunications services, replacing the previous 3% business tax.	100	Universalization of service
Thailand	7% VAT	20%. From Jan'25, certain MNCs will be taxed at 15% and companies receiving incentives from the Thailand Board of Investment can get exemptions of up to 13 years.	**Annual License Fee:** 1.5% of revenue.	**Universal Service Obligation (USO) Fee:** 2.5% of net income from telecommunications services.			Import Duty Exemptions for certain Telecom Equipment	100	Universalization of service
Indonesia	12% VAT	22%	**Telecommunications Operators Fee:** Percentage of gross revenue as prescribed by government regulations.					100	Universalization of service
Bhutan	No VAT/GST	30%	**Annual License Fee:** 1% of Adjusted Gross Revenue (AGR) or Nu. 5,000 for Class B licenses, whichever is greater.				Exempted sales tax on prepaid and postpaid telecom services as per the Tax (Amendment) Act of Bhutan 2020.	100	Universalization of service
India	18% GST	Effective 25.17% Concessional tax rate for certain domestic companies.	License Fee: 8% of Adjusted Gross Revenue (AGR)		A withholding tax of 2% is applicable to companies engaged in the business of operating call centers.		Section 80-IA(4)(ii) of the Income-tax Act provides 100% deduction of profits for 10 consecutive years for telecom services; operators have sought custom duty exemptions on telecom equipment.	74	Direct taxation without sector descrimination
Sri Lanka	8% VAT	24%		Telecommunication Levy: 15.31%; Government Levy: 2.04%	Sector-specific consumer taxes on mobile services exceed 30% of Total Cost of Mobile Ownership (TCMO).		Proposed 15% rate for foreign service providers effective April 1, 2025.	67	Direct taxation and sector specific taxation
Nepal	13% VAT	30%	License Renewal Fee: Rs 20 billion (~140 Mn USD) for 5 years	10% Telecommunication Service Charge	4% Royalty, 2% Rural Telecom Development Fund contribution	**Ownership fee:** NPR 500 per postpaid/landline connection; 2% on SIM and recharge cards		47	Service Tax Revenue Maximization
Bangladesh	15% VAT	40% (publicly traded) 45% (non-publicly traded)	Revenue Sharing: 30% of revenue. Annual License Fee: Amount varies based on license type and coverage area (e.g., Tk. 5,00,000 for nationwide Internet Protocol Telephony Service Providers).		Minimum turnover tax of 2% (higher than the 0.6% applied to other sectors)	Additional fees include evaluation and license acquisition charges.		32	Service Tax Revenue Maximization
Pakistan	19.5% Sales tax	29%	**Annual License Fee:** 0.5% of Annual Gross Revenue. **Universal Service Fund (USF) Contribution:** Up to 1.5% of gross revenue after specific deductions.		Sector-specific consumer taxes on mobile services exceed 30% of TCMO.	Advance Income Tax on telecom services (15%)		22	Service Tax Revenue Maximization

Telecom Services are lifeline – not luxury. Many industry experts including GSMA, World Bank, ICC, International Telecommunication Union (ITU) have advocated for lower taxes on telecommunication services that in turn contribute to grow digital economy and eventually result in higher government income.

Figure 4

How lower tax rates can lead to higher overall tax revenues



Source: GSMA Intelligence

"**The World Bank** has found, based on an econometrics analysis of 120 countries, that each 10% increase in broadband penetration increases economic growth by 1.3%. **– ICC paper**

Table 4: Calculation Results

Overall effect of a 20% tax increase on -	Price elasticity of demand A. Low (-0.6)	B. High (-1.2)
GDP	– 0.31	– 0.61
Tax revenues	+ 0.22	+ 0.09

out in the box above, the imposition of a 20 per cent tax on broadband will, depending on how sensitive broadband is to price, reduce GDP by between 0.31 and 0.61 per cent.

With a low price elasticity of demand, the decline in GDP of 0.31 units of GDP is compensated for by an increase in tax revenue of 0.22 units. With the higher price elasticity of demand, when the tax reduces consumption more, output falls by 0.61 units and tax revenue is only 0.09 units. This is a much poorer ratio of increased tax return to GDP cost.

Source: Taxing telecommunication/ ICT services: an overview (ITU)

TARGET 2: MAKE BROADBAND AFFORDABLE

By 2025, entry-level broadband services should be made affordable in low- and middle-income countries at less than 2% of monthly Gross National Income (GNI) per capita

According to the ITU's 2023 Facts and Figures Report, mobile broadband and fixed broadband have become more affordable in all regions of the world and for all income groups. Where data are available, 114 out of 188 economies meet the affordability target for data-only mobile broadband, up by 11 from 2022. For fixed broadband, 71 out of 178 economies meet the target, unchanged from 2022.

Also Referenced in DNF2.0 and 2025 Advocacy Targets of the Broadband Commission

To further promote Nepal's Information and Communication Technology (ICT) sector, the government has introduced several tax reforms and incentives in recent years. But this ICT cannot grow without reform in Telecom industry.

"If the ICT sector is the boat, the telecom sector is the river,"

said State Minister for ICT, Post, and Telecommunication Zunaid Ahmed Palak of Bangladesh, quoting Prime Minister's ICT Advisor Sajeeb Wazed Joy.

Employment based tax rates

- IT Industry entity providing direct employment to ≥ 100 Nepali Citizens: **22.5%**
- IT Industry entity providing direct employment to ≥ 300 Nepali Citizens: **20.0%**
- IT Industry entity providing direct employment to ≥ 500 Nepali Citizens: **18.75%**
- IT Industry entity providing direct employment to ≥ 1000 Nepali Citizens: **17.5%**

Industries established in Special Economic Zones (SEZ)

- On Foreign Technology or Management Service Fee and Royalty received by foreign investors of industries established in Special Economic Zones **- 50% concession on Applicable Tax Rate**

Tax benefits for export of services:

- Entity having income from exports - **20% concession on Applicable Tax Rate**
- Income earned in foreign exchange from export of IT services including BPO, Software Programming, Cloud Computing - **50% concession on Applicable Tax Rate**

Tax benefits for IT Parks

- Entities engaged in Software Development, Data Processing, Cyber café, Digital Mapping if established in Government specified IT Park, then such entities shall be provided tax concession **@50% on applicable tax rate**.

Abroad investments

- Following IT industry entities incorporated in Nepal shall be allowed to make investments abroad: Technology Park, IT Park, Biotech Park, Software Development, Computer and incidental services, Data Processing, Cyber Café, Digital Mapping, BPO, KPO, Data Center, Data Mining, Cloud Computing, Digital Signature Certifying Agency, Web Portal, Web design service, Web hosting, Online classified advertisement service.

Nepal’s IT sector hails ordinance passage as boost for digital future - Fiscal Nepal

Recommendation

The first step is to remove sector specific taxes in telecom sector. Second step is to consider mobile telecom a utility and apply a universalization approach.

Service Revenue Maximization from Telecom (>50% of rev) → **Direct Taxation without sector Discrimination (35-50% of rev)** → **Universalization of Service Approach (<35% of rev)**

Tax category	Current Status	Reform Suggested
VAT	13% VAT levied on all services	• No Change
Ownership Tax	NPR 500 per postpaid/landline connection; 2% on SIM and recharge cards	• Remove
Telecommunication Service Charge	10% on Voice and Data services	• Remove
Royalty	4% for Telecom Companies	• Remove as this is duplication for Spectrum paying Cellular cos.
Rural Telecommunication Development Fund	2% for all Telecom Companies	• Mandate only for companies investing <15% in rural areas • Extend scope to include loss making sites (esp highways)
Corporate tax	30% against general norm of 25%	• 25% like other companies
License fee	20 Bn NPR for 5 years	• 8% of revenue (as proposed in Draft Telco Bill) and should be applicable across the service providers incl. ISPs
Spectrum fee		• Regular Spectrum Auctions for better quality upgradation in existing band. Base Price should be revisited considering current industry status. No principle of Retrospective charging. Spectrum capping to be removed or relaxed.
Other tax reforms		• 20% Tax rebate on export of services (ILD incoming, Intl A2P, roaming)

Thank you