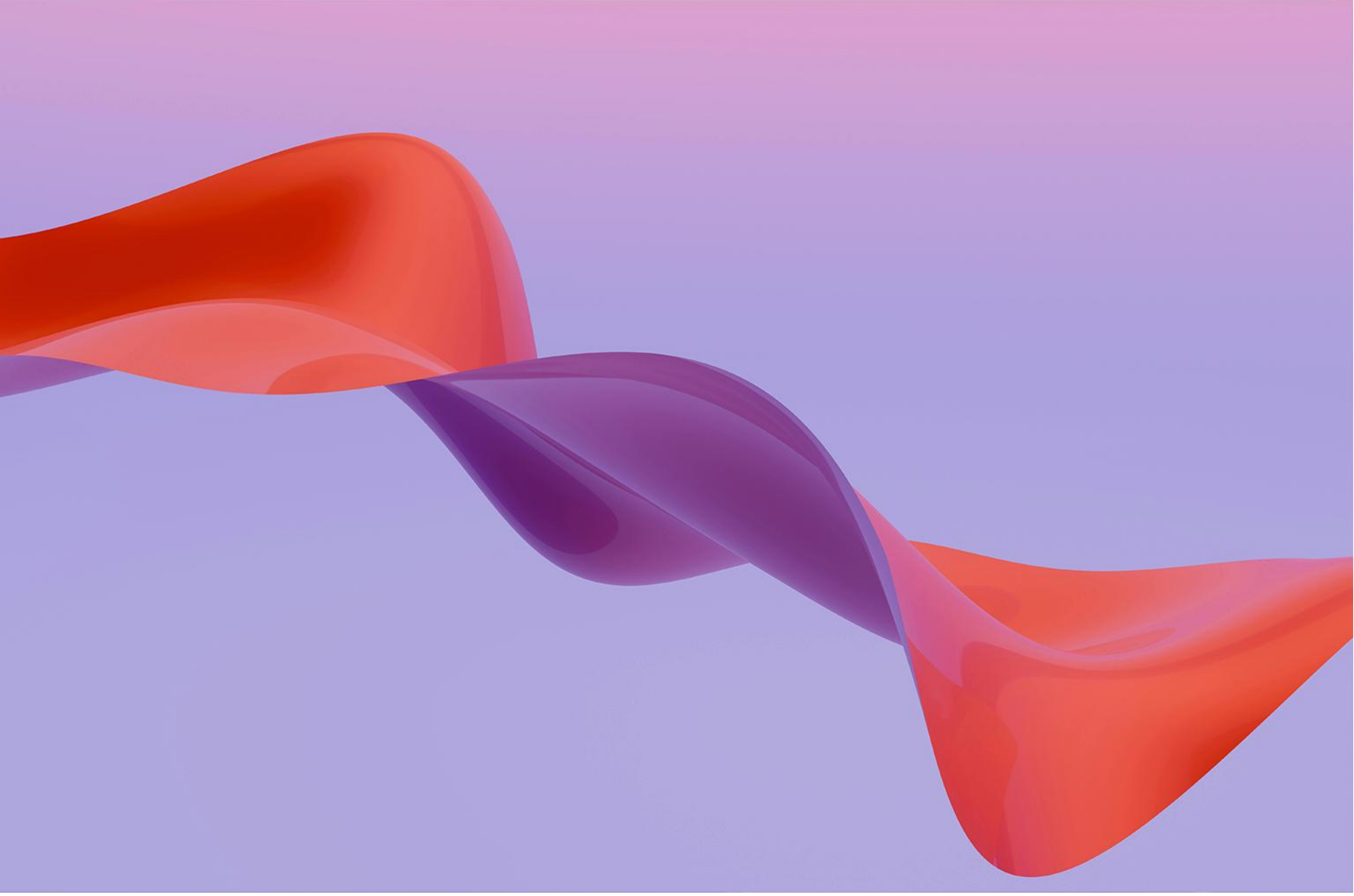

Legal Update

Finance Bill, 2082: Key Changes in Taxes

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Background

On May 29, 2025, the Finance Minister, Mr. Bishnu Prasad Paudel has presented the budget of Federal Government of Nepal for Fiscal Year 2025/26 (2082/83) along with the Finance Bill, 2025 (2082) **(the "Finance Bill")**, Appropriation Bill 2025 (2082) and National Debt Bill 2025 (2082).
Among the other Bills, the Finance Bill introduces new tax headings, tax amnesty schemes, and amendments to major tax laws of Nepal including Income Tax Act 2002 (2058), Value Added Tax Act 2052 (1996), Excise Duty Act, 2058 (2002) and Customs Act 2064 (2007).

The Finance Bill is fully effective after it is passed from both the houses of Federal Parliament, is certified by the President and published in the Nepal Gazette notification. However, some of the provisions listed in the Schedule is effective immediately (i.e., from May 29, 2025).

This update will highlight the key amendments and provisions introduced by the Finance Bill 2025, focusing on major tax incentives, procedural clarifications, and continuity in tax amnesty schemes from previous fiscal years.

Major Highlights

1) Expanded Income Tax Exemptions for IT, Hotel, and Tourism Sectors under Income Tax Act, 2002 (the "ITA")
   The Finance Bill and the Budget Speech has put special attention to promote participation of private sectors in IT, and hotel and tourism. There are several income tax exemptions and facilities provided to IT sector, and hotel and resort sector which were previously exclusive to the Special Industry only (i.e., Manufacturing industries, agriculture and agro-forestry industries and mineral industries). One of the major facilities in the Finance Bill is that it provides tax concession of 20% in the applicable corporate tax rate as per the ITA to Information Technology (IT), hotel and resort business.

2) Expansion of Income Tax Exemption for Start-Up Entities
   The Finance Bill has amended the previous facility for start-up business, making the startup entity with annual turnover up to NPR. 10 crores eligible to obtain full exemption of income tax for initial five years of operation.

3) Digital Services No Longer Subject to Permanent Establishment Regulation
   The Finance Bill has removed the requirement for a permanent establishment for non-resident (foreign) entities providing digital services in Nepal under the ITA. As a result, such

digital service providers are now required to comply with only Digital Service Tax (DST) and VAT regime in Nepal and are not required to pay profit tax under the ITA.

After the amendment, the digital service providers offering services to customers in Nepal and generating annual turnover exceeding NPR 3 million must pay a 2% DST on their annual turnover. Additionally, the Finance Act has also exempted business to business (B2B) digital services applicable to DST.

Similarly, there has been no change in requirement of registration for the VAT. The amendment to the VAT Act 1996 (2052) (the "VAT Act") has clarified some previous activities and included additional activities within the definition of digital services in the VAT Act. As such the non-resident digital service providers are required to issue VAT invoice for the fees that they charge to customers.

4) Exemption of Charges and Interests applicable in Change in Control

The Finance Bill has provisioned to waive applicable charges and interest on income tax arising from corresponding change in control in the interest held by the resident entity in another resident entity. For the purpose, such entity which is required to pay income tax from Change in Control between resident entity in Nepal shall be waived from all applicable interest and charges if it pays applicable income tax made by revised tax assessment within end of the fiscal year 2025 (i.e. July 15, 2025).

5) Continuity with Major Tax Amnesty Scheme and Tax Heading from the Previous Finance Act

The Finance Bill 2025 retains several key tax amnesty schemes and tax headings from the previous Finance Act. Notably, it continues to offer waivers on applicable interest, fees, and penalties for VAT and excise tax—provided the taxpayer settles the principal tax amount. However, the rates and eligibility criteria for these amnesty benefits under the Income Tax Act have been revised.

On the other hand, the tax amnesty scheme that previously allowed taxpayers to waive accumulated interest and penalties for failing to register under PAN—conditional upon registering for PAN and filing income tax returns for F.Y. 2021/22 and F.Y. 2022/23—has been discontinued. Further, the Finance Bill does not specifically provide any tax amnesty in cases where there is dispute under consideration of the IRD, Revenue Tribunal or Supreme Court.

6) Legal Remedies Clarified for Specific Tax Assessments in the Finance Act

The Finance Bill has introduced much-needed clarity regarding the legal remedies available to challenge tax assessments made under certain tax headings. Assessments made under 'Luxury Tax' and 'Health Risk Tax' can now be contested through an administrative review at the Inland Revenue Department. Furthermore, decisions from this review may be appealed before the Revenue Tribunal.

However, the Finance Bill still lacks general legal recourse to challenge tax assessment under other headings besides the abovementioned. For instance, the Finance Bill still has not provided any recourse against the assessment made under DST and other tax headings.

New Tax Allocation in Various Sectors under the Finance Act, 2025

1) Information Technology Sector

The Information Technology Sector has been considered with key interest in the Budget Speech 2025/26 as well as the Finance Bill. The Budget prioritizes on expanding the infrastructure and technology and scope of IT services in Nepal. For the purpose, the Finance Bill has provided various incentives and tax exemptions that encourages entities to participate in business activities of IT Sector. Following are the exemption and facilities provided from the Finance Bill in the Income Tax Act 2002 (2002) (the "ITA"):

A. **Effective Tax Rate for IT Sector:** The Finance Bill has provided IT sector eligible for incentives in tax rates. Previously, this facility was only provided to the Special Industry.

   20% of tax is reduced from applicable income tax to entity working in IT Sector of Nepal. This makes the effective tax rate of entity in IT Sector to be 20% which was previously 25%.

B. **Exemption Facility for Specific IT Industry:** Industries related to software development, data processing, cybercafe, digital mapping establishing in technological park specified by the Government of Nepal by a Nepal Gazette notification shall have 75% exemption from income tax. Previously, the exemption rate was 50%.

   As the Government of Nepal has not published Gazette notification to designate the technological park yet, the provision remains practically ineffective.

C. **Expansion of Income Tax Exemption Facilities for Start-Up Industries:** The Finance Bill has expanded the scope of start-up businesses by allowing those with an annual turnover up to NPR 10 crores to claim an income tax exemption for the first five (5) years of operation.

Previously, the facility was limited to startup business with annual turnover of NPR 1 crore. However, as per the ITA, the facilities can only be utilized by start-up industries as defined by the notification of Inland Revenue Department ("IRD").

D. Income Tax on Export of IT Services: The Finance Bill has mentioned that the final withholding tax of 5% shall be levied on the income of person, exporting information technology services abroad.

E. Digital Service Provider: The Finance Bill has removed the applicability of permanent establishment for foreign entity providing digital services in Nepal. Previously, a foreign entity was considered under permanent establishment in Nepal if it

(a) has a significant digital presence in Nepal, or,

(b) conducts transactions in Nepal involving data or services for at least 90 days within the last 12 months while keeping a server outside of Nepal ("Digital PE").

After the amendment, the Digital service providers offering services to customers in Nepal and generating annual turnover exceeding NPR 3 million must pay a 2% DST on their annual turnover.

However, the Finance Bill has not provided any legal recourse to challenge the reassessment made by the tax officials under the DST. For instance, if the tax officials reassess the liability under DST after the person has declared and submitted the DST then the person no legal recourse to challenge the reassessment under the Finance Bill.

In relation to amendments to the VAT Act, there has been no significant changes in the applicable conditions of VAT on digital services although there have been few additional business activities included in the digital service.

2) Transportation Sector

A. **Exemption of Tax for Old Public and Private Vehicle:** The Finance Bill has introduced a provision to grant the remaining income tax exemption to public and private vehicles older than 20 years or those who do not come into operation, for the purpose of deducting their income tax of last two years.

B. **International Civil Aviation Provider and Ticket Seller:** The Finance Bill has waived applicable interest, charges, and additional fees until fiscal year 2025 for entities that register for VAT and pay the applicable VAT on services from fiscal year 2023 by the end of fiscal year 2025.

C. **Continuation of Tax from Previous Fiscal Year:** The Finance Bill has carried over with certain tax headings from previous fiscal years. As per Bill, concerned person is required to pay green tax, road construction fee, road maintenance and improvement fee, pollution control charges.

D. **Claim of Rental Expense Paid to a Natural Person:** The Goods Transport Service Provider who have rented vehicles from natural persons may claim the rental expenses for fiscal years 2023/24, 2022/23, and 2021/22, provided that Tax Deducted at Source (TDS) was duly withheld on such payments.

3) Renewable Energy Sector

A. **Electric Charging Machines:** An entity manufacturing and assembling charging machines for electric vehicles shall obtain full income tax exemption for the initial 5 years from the date of operation.

B. **Production of Green Hydrogen:** Similarly, an entity producing green hydrogen shall obtain full income tax exemption for the initial 5 years from the date of operation.

4) Hotel & Resort Sector

A. **Effective Tax Rate for IT Sector:** Similar to IT Sector, the Finance Bill has provided hotel and resort sector with incentives in the applicable tax rates under ITA. As per the facility, one third of tax is reduced if the natural person falls within the tax bracket of 30%. This makes the effective tax rate for the person to be 20%. Similarly, 20% of tax is reduced from applicable income tax to entities. This makes the effective tax rate of entity in IT Sector to be 20% which was previously 25%.

B. **Waiver of Income Tax Based on Number of Employment and Location of the Industry:** The hotel and resort has been included with IT sector and special industry to obtain waiver of income tax based on its rate of employment of people and location of the industry. The following provides the list of tax waiver facility:

a. Based on Number of Employees

Entities	Incentives
100 or more Nepalese nationals throughout the year	The tax is applicable only 90% of the applicable rate in such income year
300 or more Nepalese nationals throughout the year	The tax is applicable only 80% of the applicable rate in such income year
500 or more Nepalese nationals throughout the year	The tax is applicable only 75% of the applicable rate in such income year
1000 or more Nepalese nationals throughout the year	The tax is applicable only 70% of the applicable rate in such income year

100 or more Nepalese nationals throughout the year including 33% women, Dalits or handicapped	Additional 10% exemption in applicable rate

C. **Requirement for Five Star Hotels & above and luxury hotels to file Luxury Taxes:** The Finance Bill has increased the applicability of luxury tax for hotels of five star & above and luxury resort. Upon the inclusion of luxury tax, two percent tax is levied on the sales price of services provided by luxury resort, hotel of five star and above. The luxury tax is levied directly on the revenue stream of the business.

Special provision for Waiver of Dues & Relief

The major tax amnesty schemes which have continued this fiscal year includes waiver of certain applicable interest, fees and charges under income tax, VAT and excise tax if the taxpayer complies with certain provisions. However, there has been certain change in the eligible conditions and relief under the current Finance Bill.

Here is the updated list of the special provision related to Dues and Relief:

A. **Waiver of applicable charges and interest under Change in Control from onshore transfer of shares:** A resident entity which is required to pay income tax from Change in Control from onshore transfer of shares between resident entity in Nepal has been waived from all applicable interest and charges if it pays applicable income tax made by revised tax assessment within end of the fiscal year 2025. (i.e., July 15, 2025). This provision does not facilitate Change in Control occurring from offshore transaction.

B. **Failure to submit income tax returns:** A person who receives a revised tax assessment from the tax office for failing to file an income tax return will be exempt from the additional tax liability under that revised assessment—provided they file the overdue return and pay the due income tax for that fiscal year by January 2026. However, this waiver is not applicable to income tax reassessment in the tax headings of income tax returns filed by the person.

C. **Failure to submit VAT until the F.Y. 2024/25:** A person who failed to register under VAT and VAT returns for the period until the fiscal year 2024/25 shall obtain wavier of all fines, fees and remaining interest if the person submits VAT returns and pay twenty five percent of the applicable interest thereon, within January 2026. The person had to submit VAT returns and pay fifty of applicable interest to receive the waiver under the tax amnesty scheme as per the previous Finance Act 2024.

D. **Failure to submit Excise Duty until the F.Y. 2024/25:** A excise license holder who failed to determine and collect excise duty until the F.Y. 2024/25 shall obtain waiver of all fines and delay charges if the excise license holder submits the excise duty return and fifty percent of applicable delayed charges within January 2026.

Similarly, a person who has already filed the excise duty return for the fiscal year but fails to provide the excise duty shall also obtain waiver of all fines and delay charges if it submits the applicable excise duty within January 2026.

Major Tax Amnesty Schemes and Tax Heading Revoked from the previous Finance Act

While major tax heading and tax amnesty schemes are retained from the previous Finance Bill, there are some provisions which have been revoked and discontinued:

1) **Tax Amnesty Scheme for Person doing taxable transaction without obtaining PAN**
   The tax amnesty scheme provided to person doing taxable transaction without obtaining PAN has been removed in the Finance Bill. In the previous Finance Act 2024, a person who is conducting taxable transactions without obtaining the PAN were eligible to obtain waiver of all applicable tax before F.Y. 2021/22 if the person registered under PAN, filed income tax returns for F.Y. 2021/22 and F.Y. 2022/23 and paid the taxes thereon within March end of 2026.
2) **Approved Social Security Fund**
   The concept of approved social security fund approved by the Inland Revenue Department has been removed from Finance Act and Income Tax Act. As per the Finance Bill, the retirement funds approved from the Inland Revenue Department must obtain affiliation with retirement funds established under the existing Nepalese laws which includes Employer Provident Fund, Citizens Investment Trust, Pension Fund or Social Security Fund.
3) **Advance Tax Deduction at Customs Points**
   The Finance Act 2023 had introduced a provision for advance tax deductions at customs points on various imported goods, including live animals, meat, dairy products, and other essential goods. This provision has been removed from the Finance Bill.
4) **Permanent Establishment on Digital Service Provider**

The Finance Bill has removed the applicability of permanent establishment for foreign entity providing digital services in Nepal and has limited the applicability of DST in business to consumer activities (B2C) and not in business-to-business activities (B2B).