Privatization Prospects

in

Nepal

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Abbreviations

ADB	Asian Development Bank
AKA	Also Known As
BYS	Balaju Yantra Shala (P) Ltd.
CEO	Chief Executive Officer
FRG	Federal Republic of Germany
HMG	His Majesty's Government
IDA	International Development Association
JCF	Janakpur Cigarette Factory
NIC	Rastriya Beema Sansthan
NIDC	Nepal Industrial Development Corporation
NOC	Nepal Oil Corporation
NPC	National Planning Commission
NRB	Nepal Rastriya Bank
NTL	National Trading Ltd.
NYSE	New York Stock Exchange
PRC	People's Republic of China
PSC	Public Service Commission
SATA	Swiss Association for Technical Assistance
SEC	Securities Exchange Centre Ltd.
SOE	State Owned Enterprise
USAID	United States Agency for International Development
USSR	Union of Soviet Socialist Republics

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"Public enterprises are hybrid institutions created with the expectation that the strengths of the private sector will be combined with those of the public sector... By combining the strengths of both, public enterprises were expected to do the right things and to do things right. Unfortunately, this experiment in genetic engineering seems to have failed."*

Dr. Prajapati Trivedi
Professor of Public Enterprise
Indian Institute of Management Calcutta

* India Today June 30, 1987, page 64

CHAPTER I: INTRODUCTION

A. Scope of Work

This study was commissioned by the USAID Mission/Kathmandu in August 1987. Work began on October 15, and the draft final report was presented to the Mission on December 11. The contractual scope of work called for:

1. An analysis of the various laws and regulations governing operation of private enterprise to determine incentives, disincentives, overlaps.

2. An anlysis of the various laws and regulations governing operation of parastatal enterprises, e.g. wage scales, sources of management, procurement regulations, reporting requirements, etc. to determine possible incentives/ disincentives to divestiture.

3. Identification of the Government's portfolio of businesses including the responsible ministry, the holding companies, the operating companies, the subsidiaries and the financial inter-linkages.

4. Identification, as may prove possible, of sectors where the Government is contemplating further business expansions or diversifications and, the external sources from which it may be seeking financing/technology therefor.

5. Analysis of the various laws and regulations governing the operations of the Securities Exchange Center and, as may prove relevant, commercial banking and other financing institutional activities.

6. A preliminary investigation of the private sector's receptivity/capacity to absorb non-traditional financial instruments.

B. Parameters

While not explicitly stated in the scope of work, the study's overall objective was the identification of obstacles to privatization of His Majesty's Government's productive public enterprises. In principle, privatization has been a specific objective of HMG at least since adoption of the Seventh Five Year Plan in 1985. In practice, it has meant the - generally unsuccessful - offering of a small minority of shares in - generally unsuccessful - public enterprises. As of the time the study was conducted there were informal indications from HMG officials that the failure of such efforts was recognized, and that a broader and more specific statement of privatization policy was imminent.

In the absence of such statement, there continue to be significant differences of definition within HMG not only as to what constitutes "privatization" but even whether a given entity is or is not a "public" enterprise. It has, therefore, been necessary for this study to establish its own parameters.

There can be little argument that privatization has been one of the major issues of the 1980s, whether in nations termed developing or developed. Any reading of the existing literature makes clear that the underlying forces are many and that their priority varies significantly from country to country.

His Majesty's Government, however, has repeatedly stated its objective of improving the efficiency of Nepal's public enterprises. That is the economic rationale for privatization in the most straight-forward terms*. For that reason, reference to the experience of other countries (where shifting ideologies, changing political leadership or concern over government size may be critical to the privatization debate) seems largely irrelevant to this study. However, it is not to imply that HMG is unaware of the direct benefits that may accrue to a selling government: reduced demands on the central budget or for government borrowings or guarantees; new revenue sources; fewer distractions from more traditional areas of government responsibility.

Finally, the prospective benefits from privatization are implicitly considered in terms of financial profitability rather than economic or social profitability - because that is the author's background (and because the precision of the latter measures is increasingly subject to debate).

The study focuses on public enterprises as distinct from public services. This is not meant to suggest that there is necessarily a clear line of demarcation between the two, nor that public service sectors (e.g. transport, communications, health care) are unsuitable candidates for privatization. Further, the trading sector in general and organizations such as the Agricultural Inputs Corporation and Nepal Food Corporation in particular have not received extensive consideration (which, inter alia would duplicate work already done by the World Bank, ADB, etc.)

As a matter of definition, privatization in this study means sale of 51% or more of the outstanding equity capital from government (or parastatal organizations) to the private sector with concurrent transfer of control of the entity's board of directors and management. A further required ingredient in specific instances may be the withdrawal or elimination of government controls which ispo facto can determine financial viability.

There is at least one other arrangement frequently included under the heading of privatization wherein government retains ownership

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* There are scholars who would and do argue that "private" does not necessarily equate with "more efficient". But, in the 1980's they are a clear minority.

of most or all of the assets, but transfers management responsibilities to the private sector. This has a long history in many developing countries in areas such as airlines and international class hotels. While broader application would certainly appear feasible, there are few if any discernable trends in that direction. This study will, therefore, address only issues where permanent transfer of all controls (ownership, board and management) are involved. Parenthetically, privatization does not by definition imply the end of all government involvement in productive sectors of the economy. Private companies presumably will continue to seek financial assistance from government-supported credit institutions and government guarantees on external loans where required by international lenders.

There would be no useful purpose served here in any lengthy recital of the constraints (purchasing power, access to markets, infrastructure, population pressures, lack of exploitable natural resources, etc.) to Nepal's growth and development. These are economic "givens". There is one non-economic constraint, discussed hereafter, which warrants identification here. It is that government policies are viewed not only by the private sector but also by public sector managers as confusing, conflicting and/or irrational.

These feelings are endemic; they will not vanish with the announced privatization of one or more public enterprises. In fact, a likely reaction could well be suspicion as to the government's true motives in divesting itself of the enterprise in question. Time and patience will be required.

The study itself begins with a brief chapter describing the creation of public enterprises over the past 30 plus years, and is followed by a section devoted to the current situation. The manufacturing sector receives primary attention. There follow brief descriptions of five public enterprises. Each of these profiles is based on personal interviews with senior management, and is believed factually accurate. Not all pertinent information is, or could be, included. Other data might have seemed more germane to other authors. The object in each instance is to raise a single question: does this enterprise now belong in the public sector? Answers will presumably vary depending on the reader's orientation.

There follow sections on various current constraints to privatization grouped under three broad headings: statutory; financial; and, seeming HMG concerns. And, ultimately, conclusions and recommendations.

Finally, very considerable field time was devoted to identifying the laws and regulations that govern operations of public and private enterprises in Nepal. These are listed in Appendix C together with summaries of, and issues raised by, the principle statutes. Appendix D list another 50 enactments also bearing on company operations that were reviewed but not found sufficiently critical for detailed description.

Equal attention was given, as is also called for in the scope of work, to identifying those companies in which HMG has a financial interest. We are reasonably confident that Appendix A, which details enterprises with an HMG holding of 51% or more, is complete. However, there may well be errors or omissions in Appendix B, which lists HMG direct and indirect holdings totalling 50% or less. It might be noted that, despite numerous official representations to the contrary, we were unable to identify any single repository of data for Appendix B.

C. Acknowledgements

The sources of information for this study were numerous and, without exception, cooperative. The author would like to express his appreciation, as well as to acknowledge specifically the invaluable assistance of his research associates:

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Errors of fact or interpretation are solely the author's responsibility.

CHAPTER II: PUBLIC ENTERPRISES - A BRIEF HISTORY

A. First Four Plans (1956-74)

In 1956, when the First Five Year Plan was introduced, there was exactly one public enterprise (Nepal Bank Ltd.) in the country. By 1974, the final year of the Fourth Plan, there were 61 (subsequently reduced by the sale of Nepalese Carpet (P) Ltd. and the Vegetable Ghee Company). Of the net total, 37 had been established under the Company Act, six under the Corporation Act, four under the Communication Corporation Act, two each under the Commercial Bank Act and the Development Board Act and eight by special charter. Eight different ministries and the NPC were responsible for their supervision*.

In the total were a considerable number of industrial estates, rice and other commodity trading companies, development authorities (e.g. NIDC, Cottage Industry and Handicraft Emporium, Agriculture Development Bank), etc. However, 15 of the 25 SOEs assigned to the then Ministry of Industry and Commerce were in the manufacturing sector. Of these, the largest (authorized capital of Rs. 10 million or more) were:

Enterprise	Date Established	Authorized Capital	External Assis-tance	Ownership
		Rs million		
Bansbari Leather	1962	Rs 10	PRC	HMG-100%
Birgunj Sugar	1964	100	USSR	HMG-100%
Janakpur Cigarette	1966	80	USSR	HMG-100%
Brick & Tile Factory	1968	20	PRC	HMG-100%
Agricultural Tools	1969	30	USSR	HMG-100%
Himal Cement	1970	20	FRG	NIDC/ NTL-100%
Royal Drugs	1972	15	None	HMG 92% NIDC 8%
Hetauda Textile	1974	100	PRC	HMG 100%

Combined authorized capital of the remaining seven manufacturing enterprises (excluding only the private Raghupati Jute Mills which HMG acquired in a 1959 salvage attempt) totaled a mere Rs.

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* Profiles of Public Enterprises in Nepal, Office of Corporation Co-ordination Council, 1978.

13.7 million. Thus, in terms of authorised capital (admittedly a crude measure but sufficient for illustrative purposes), Rs. 360 million of Rs. 389 million (93%) of new investment in public sector manufacturing during the years 1956 through 1974 was directed to just eight enterprises.

Six had been built with the assistance of either the PRC or the USSR, one with FRG help and one converted from an HMG department. Ownership, understandably, was vested exclusively with HMG. A 1977 study stated that these enterprises "can be identified as the direct off-springs of foreign aid (mainly grants). In them, the role of foreign aid was absolute in bringing these industries under the public sector"*.

Other bilateral and multilateral donors were, of course, also active in Nepal during these years, but their concentration tended toward other sectors of the economy (or, if to industry, through support functions such as industrial estates and development finance). To cite specific examples, the Nepal Electricity Corporation, the Drinking Water and Sewerage Board, the Nepal Telecommunications Corporation, the Jute Development Trading Corporation, the Dairy Development Corporation, the Timber Corporation of Nepal Ltd. and the Transport Corporation of Nepal had all existed as small government departments prior to being transformed into legal entities to receive or channel foreign aid. Donors included IDA (The World Bank), ADB, USAID, Japan, the Netherlands, New Zealand and Denmark as well as the PRC and the USSR.

B. The Fifth and Sixth Plans (1975-84)

In 1974, HMG announced a new industrial policy. Industries were classified in terms of fixed capital investment into four broad categories:

1) Cottage and rural - upto Rs. 200,000;

2) Small scale - Rs. 200,000 to Rs. 1 million;

3) Medium - Rs. 1 million to Rs. 5 million; and,

4) Large scale - over Rs. 5 million.

With regard to the role of public enterprise in manufacturing per se, it was stated that for the future:

> 1) In basic industry (defined as iron and steel, chemical fertilizers, petroleum and cement), HMG reserved the right to subscribe from 51% to 100% of the paid-up capital in any such enterprise,

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* Performance of Public Enterprises in Nepal, Office of Corporation Co-ordination Council & Industrial Services Centre, 1977.

2) In primary consumer goods (defined as cotton textiles, medicines, dairy products, vegetable oil/ghee, writing/printing paper), HMG might initiate such an enterprise but not necessarily retain as much as 51%, and

3) In other primary consumer sectors (not defined), HMG might initiate but would subsequently dispose 100% to the private sector.

As noted earlier, there were a net 59 public enterprises as of the end of the 4th Plan. The number of new SOEs proposed during each of the 5th and 6th Plan periods dropped sharply. Of the total (16), one was the Security Marketing Corporation (now the SEC), another was the Nepal Institute of Standards and seven were industrial estates. The remainder were:

Enterprise	External Assistance	Current Status
Hetauda Cement	ADB	Plant commissioned in late 1985; operating problems continue.
Hetauda Leather	See Status	Subsequently converted into joint venture with West German firm. Recently reported to have suspended operations.
Bhrikuti Paper	PRC	Trial production began mid-1986, continuing supply/demand problems.
Nepal Magnesite Industries [now Nepal Orind Magnesite (P) Ltd.]	India/IFC	Established in 1979 as a joint venture. Full scale operations projected for mid-1988.
Ganesh Himal Lead A.K.A. Nepal Metal Co.	India/IFC	Established in 1979 with projected operations in 1985. If completed, commercial operations not expected before 1991.
Udayapur Cement	Japan	Financing agreement signed October 1987.
Rosin and Turpentine Company	USSR	Plant completed in 1986. Supply/marketing problems being encountered.

As of late 1987 four factories had been completed but for varying reasons none of the companies have been able to establish commercial operations. A fifth, Nepal Magnesite, has encountered continuing financing problems which have nearly tripled project costs from original estimates. Projected capital costs of Nepal Metal have risen six-fold since the original feasibility study. Given current world zinc prices, financial viability may be in question. Construction of the Udayapur Cement Plant obviously can not begin until 1988 at the earliest.

Nepal, by 1985, according to the NPC, was approaching self-sufficiency (on a current-demand basis) in consumer items such as cigarettes and matches, some food stuffs (sugar, wheat flour, biscuits, confectionery, vegetable ghee, noodles, beer, alcoholic beverages) and laundry soap as well as paints, polyethene pipe and corrugated sheeting, but remained seriously deficient in areas such as cement, textiles and paper.

C. Seventh Plan (1985-90)

New SOE industrial projects in the 7th Plan are notable by their absence. The program calls for a) maintenance of established public enterprises, b) expansion of the Himal and Hetauda Cement plants' productive capacities, and c) completion of Bhrikuti Paper, Nepal Orind Magnesite, Nepal Metal, Lumbini Sugar, Nepal Paper and Butwal Spinning Projects. (The latter four having been approved during, but were not formally included in, the previous plans.)

The 7th Plan does identify over 100 priority industries (with estimated investment costs and physical output capacities) to be promoted in the private sector.

CHAPTER III: CURRENT SITUATION

A. Public Enterprise Policy Under the Seventh Plan

The 7th Plan points out that while only four new public enterprises had been established in the preceding five year period, the flow of funds from HMG to its SOEs had increased by an annual rate of 76%. Further noted was that the cumulative loss (as of 1981/82) had reached 40% of the SOEs' total equity. The Plan attributed this "dismal picture" to 1) the SOEs' inability to institute internal controls and 2) the negative effect of government price-fixing.

To meet overall objectives in general and increased private sector participation in particular, the Plan adopted 14 policies regarding SOEs. Some were directed at HMG ministries, others at public enterprise managements. Some were highly specific; in other cases, targets were only vaguely defined.

HMG is now approaching its mid-term review of Plan accomplishments. The table below reflects discussions with officials in various ministries as to the current status of the public enterprise objectives. The division of the implemeatation efforts into categories of (1) accomplished (2) attempted and (3) neither accomplished nor attempted is the author's effort to convey a reasonable concensus of these officials' views. While necessarily a bit arbitrary, the author believes that no HMG official interviewed would argue that any of the items in category (1) belonged in (2) - or vice versa*.

Policy No. Accomplished	Objective
5	Accountability of SOE chiefs clearly defined: to be appointed; rewarded; and punished on this basis.
6	Product quality-control standards to be established for SOEs with monopoly rights.
7	A plan to be prepared to assure organized supply of essential goods.
11	HMG to financially assist an SOE if losses result from HMG decisions in the national interest.

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* The policy objectives are summarized here, the full text can be found by the number reference in pages 246 and 247 of the Plan.

13	SOEs to be classified as to whether expected to earn profits, to run at break-even or to be subsidized.
Attempted	
3	SOE boards of directors to set salaries, allowances, appointments and promotions, product prices, and capital investment programs.
9	SOE shares to be floated widely to mobilize savings.
10	SOE's to submit financial statements within 6 months of fiscal year end.
12	Each concerned ministry to establish a separate unit to monitor SOE performance.
15	SOE management incentive system to maximize profits/minimize waste against set targets.
Neither	
1	Additional amalgamations of similar SOEs.
2	Prepare list of financially unviable SOEs and effect process of amalgamation, liquidation or transfer of ownership.
8	Give priority to industrial enterprises that will contribute to goal of self-sufficiency.
14	Encourage private sector participation in SOEs being run on government subsidy.

With regard to the policies in the mid-range "attempted but not accomplished" category:

- SOE boards of directors do fix allowances (except in subsidized enterprises), but wages and salaries remain set according to PSC regulations. Boards do not move to confirm appointments; some SOE managers have been in "acting" capacities for as long as six years. Boards do not exercise independent responsibility for product pricing.

- A few shares in a few SOEs have been offered; there has been no savings mobilization impact.

- Few SOEs come anywhere near the six-month submission target.

- There are individuals within the ministries who now monitor SOEs, but discreet units have not been created.

- The Cabinet in 1985 established detailed performance criteria, but the financial rewards due successful SOE managers remain undisbursed.

B. Structural Adjustment Plan Objectives

As part of the Structural Adjustment Plan arrangement between HMG and the World Bank it was agreed, _inter alia_, that more realistic pricing policies would be adopted for public enterprises, managements strengthened and the size of the public sector reduced through the process of divestiture.

Such objectives are clearly in full consonance with HMG's own policies as expressed in the 7th Plan. However, among the specific measures called for in conformance with the World Bank's initial loan was formulation of an action plan for closure, divestiture, and management reforms of public enterprises. As with similar provisions in the Plan itself dealing with troubled SOEs, this condition remains essentially unfulfilled.

This matter was discussed during recent visits of a World Bank mission on the subject of the second installment under the Structural Adjustment Credit. HMG proposed essentially a negative list, i.e. certain sectors of the economy in which the public enterprises would not be candidates for divestiture. The sectors were utilities, public welfare, finance and national monopolies. If this becomes official HMG policy, it seems probable that the World Bank will not require a "positive" list of specific candidates for privatization. The Bank will, however, continue to be concerned about the specifics of implementation.

C. Public Enterprises in Operation

The number of public enterprises currently operating in Nepal varies according to definition and source. Whatever the total, it is clear that principal growth period for SOEs began in the late 1960's and culminated in the early 1970's. Thereafter, the momentum to create new SOEs virtually disappeared - with the sole exception of the manufacturing (inclusive of industrial estates) sector.

There are today some + or - 25 industrial SOEs (again, the number may vary by definition or source) in operation or under construction in Nepal*. With rare exception, the larger units (in

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* There is also a relatively recent trend - discussed hereafter - of investing in operating subsidiaries whose ownership structure may differ from that of the parent company.

terms of cost, employment or other measures) have been built with foreign aid, the PRC being the most active single donor.

By the opening of the 7th Plan - which as noted forecast no new industrial SOEs - some of the longer-established factories (e.g. Janakpur Cigarette, Birgunj Sugar, Himal Cement, Bansbari Leather) had reached levels of physical output reasonably close to theoretical plant capacity. For others, including plants in trial production or under construction, the future does not appear particularly promising.

In 1983 the Centre for Economic Development and Administration at Tribhuvan University published a study based primarly on questionnaires/interviews with 59 middle and senior managers in nine of Nepal's larger public enterprises*. Among findings (presented arithmetically in the study, here in percentages) were:

1) As to why their enterprise was failing to meet targets, over 40% listed the principal cause as government policies. This becomes even more striking when compared to the next most frequently cited problems which were resource limitations (24%), market restrictions (14%), environmental factors (12%) and technology (5%).

2) Only 12% of those interviewed felt that appointment of top management was based on merit; 14% said the basis was political and 69% felt both factors were involved.

3) As for the "consequences for hard and sincere work", 29% expected appreciation and recognition and 22% a better chance of promotion. But, 25% felt that nothing particular would happen and 24% believed "nobody will care".

4) Regarding the basis for promotion, 34% listed either qualifications or hardwork. However, 39% believed years of service most important, while 27% cited "personal connections and flattery".

A more detailed examination of the causes of low efficiency in public enterprises gave the managers an opportunity to rank 14 specific factors offered by CEDA. Of the 59 managers interviewed, 45 selected the most serious problem as being either "nobody affected (by) losses" or "rules and regulations interfere

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* _Management Problems in Public Sector Manufacturing Enterprises in Nepal_, CEDA, July 1983. The public enterprises were: Janakpur Cigarette, Birgunj Sugar, Bansbari Leather, Hetauda Textile, Royal Drugs, Dairy Development, Harisiddhi Brick & Tile, Livestock Company, and Agricultural Tools Company.

in making quick decisions". It is further noteworthy that of the 14 choices, those that might seem potentially intractable problems (e.g. excess job security, lack of experienced personnel, indiscipline in the work force) ranked towards the bottom of management's concerns. The five most serious constraints all related in one way or another to the enterprise being run by or as if it were a government department.

The study findings have been discussed with the present management of some of the same public enterprises. For them, obviously, the topic is one of very considerable delicacy. When asked to compare their current operating environment to that at the time of the study, they state with apparent conviction that there have been improvements. Board chairmen no longer routinely move on after a year or two in office. Internal promotion based on merit is more common, at least among the more successful companies (which tend to have greater operational autonomy). On the other hand, it remains exceedingly rare for a CEO to have come up through the ranks.

There is no question but that HMG in recent years has attempted to encourage/enforce more management discipline in public enterprises. As noted, by a 1985 Cabinet decision every CEO is to be evaluated annually and graded on a set of established criteria (physical/financial targets, capacity utilization, return on capital employed, control on cost price, return on sales, productivity, and management development). Those managers, who have exceeded profit targets (or minimized losses) are to be rewarded by promotion and/or bonuses (up to Rs. 100,000 in principle, but not in practice). Managers, who miss targets by 25% or more are to be removed.

Controls over product pricing have, in theory, been liberalized. All public enterprises are, according to the Seventh Plan, grouped in one of three categories: those operating under competitive marketing conditions; those operating under monopoly conditions; and, those operating under HMG subsidies. For companies in the first category "HMG will not control the selling prices. The board of directors of the corporation will have full authority and responsibility in this area*." In point of fact, this simply does not happen. No public enterprise board would be rash enough to revise pricing structures absent prior consultation with its administrative ministry - a fact of life admitted both by company managers and HMG officials.

This had led to situations where remedial measures such as management evaluations and decentralized pricing can, ironically, encourage enterprises in the direction of reducing profitability. For example, a company anticipating a strong financial year may, in the spirit of "social justice", decide to pay above-market

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* The Seventh Plan, pps. 267-268.

prices to its input suppliers. This can also serve to protect management in the event of less profitable operations some time in the future. A more prevalent example is the reluctance, for fear of potential disruptions elsewhere, to consider offering above minimum wage payments in return for increased productivity.

In other words, public enterprise managements, while theoretically functioning in more of a risk/reward environment, continue to waver between financial and social objectives.

CHAPTER IV: PUBLIC ENTERPRISES - SELECTED EXAMPLES

As described in the Introduction, no attempt has been made either to undertake or to present a definitive study of the five public enterprises in this section. To the contrary, the objective is to provide capsule descriptions illustrating both the range of company activities and the channels by which HMG has become involved.

Of the five SOEs, one has been in business for over 25 years and has never been profitable. A second is under construction. All of the remainder - one in industry, one in trading and one in services - are currently profitable. All three are effectively HMG monopolies. For two, 1987 will mark the beginning of meaningful competition from the private sector.

A. Balaju Yantra Shala (P) Ltd.

1. Background

Balaju Yantra Shala (P) Ltd. (BYS) was established in 1961 by NIDC but more particularly as an engineering workshop to help construct the cheese factories that Swiss aid (presently, Swiss Association for Technical Assistance) had planned in Nepal's mountainous regions. To this day, BYS considers itself - and with pride - as a service and training center. Managemment believes that more than 60% of Nepal's present workshops (there were none 15 years ago) are operated by ex-BYS employees. BYS tries to keep one step ahead - in terms of technical complexity - of its competition; when they catch up, BYS moves on. Ten years ago BYS developed a turbine-making capability, and at least once successfully competed for an overseas tender. Today, seven other companies (five owned by former employees) copy its design and manufacture turbines.

2. Operations

BYS has no standard products, no proprietary line of its own. It makes or repairs spare parts, steel fabrications (suspension bridges, roof trusses, tanks, etc.) and office furniture and equipment as per client specification or design. Not surprisingly, BYS loses money and equally, therefore, cannot maintain the unfinished steel inventories that would make it more competitive (for, say, donor construction projects) and more profitable.

Until 1984 the company had three divisions: mechanical; electrical; and, sanitary. The latter were converted into public limited companies (Balaju Yantra Shala Electric Company Ltd. and Balaju Sanitary Engineering) and the sanitary company sold to the public via SEC share offering.

3. Current Status

BYS is presently owned 15% by NIDC, 85% by SATA. Of its five member board of directors, three (including the Chairman) are appointed by SATA, two by NIDC.

The company estimates Nepal's annual structural steel requirements (normal demand plus major projects) at 10,000 tons. BYS has a capacity of 1,000 to 1,200 tons. It estimates its competitors' combined capacity at 5-6,000 tons annually. All operate well under capacity because the principal buyers are HMG and donor aid projects which include steel from Japan, Korea, India, etc.

B. Butwal Spinning Mill

1. Background

When in 1982 the decision was made to establish an independent spinning mill in Nepal, HMG had hoped to negotiate a grant package from some donor country. Failing that, HMG in 1983 agreed to purchase the machinery component from the PRC on concessional terms (7%, eight year loan), and thereafter turned to SOEs to provide funding for the factory building, warehouses, etc. A decision was also taken to offer Rs. 32.2 million shares to the general public.

However, Salt Trading Ltd., subsequently offered to buy 31.1% of the equity and see to underwriting the balance. In early 1987 the proposal was accepted and management of the company was turned over to Salt Trading.

2. Current Status

The present shareholders of Butwal Spinning are:

Holder	Capital (rounded)	% of total
Janakpur Cigarette	Rs 32.8 million	36.5
Salt Trading	32.2	35.8
Birgunj Sugar	8.5	9.5
Himal Cement	8.5	9.5
NIDC	6.0	6.7
HMG	1.7	1.9
Cottage Industry & Handicraft Emporium	0.1	0.1
SEC	0.1	0.1
	Rs 89.9 million	100.0 %

The SEC is currently preparing a prospectus in anticipation of a public offering within the next three to four months. A limit, not yet established, will be placed on the number of shares that can be purchased by any single applicant.

The plant itself is about one year behind schedule. Machinery installation has yet to begin, employment requirements have not been established, trial production is targeted for sometime in calendar 1989. The company will buy its raw materials locally from the Cotton Development Board and internationally from leading polyester suppliers such as Korea. The purchase price of cotton and the selling price of finished yarns will be set by HMG. Prospective customers include the Cottage Industry and Handicrafts Emporium as well as the integrated textile mill.

C. Janakpur Cigarette Factory

1. Background

Janakpur Cigarette (JCF) began operations in 1964, as a "turn key" project (USSR grant aid) with an initial productive capacity of 2,000 million pieces per year. Using exclusively retained earnings, the company has increased annual capacity to 6,000 million. Some 60-70% of tobacco requirements are purchased from India with the balance provided by local farmers.

2. Operations

With the exception of two very small private companies, JCF had the domestic cigarette business to itself until earlier this year when Surya Tobacco's plant (annual capacity 900 million) went into production. Surya, (owned 49% by Nepali private interests, 49% by Imperial Tobacco of India and 2% by British American Tobacco) currently markets 4 brands as compared with JCF's 7, but across-the-board competition is expected eventually.

3. Current Status

JCF, in turn, is establishing a new company, the Seti Cigarette Factory (annual capacity 600 million), which will be sited in Western Nepal and serve that market's demand for the cheaper cigarette brands (current pricing policy does not factor in distribution costs). Seti will have an issued capital of Rs. 45 million and initially be owned 51% by JCF and 49% by 5-6 private interests, with plans for a future offering to other investors.

D. Nepal Oil Corporation

1. Background

Nepal Oil Corporation (NOC) was established in 1970 as a petroleum product retailer for India Oil. In 1973 India Oil and the two other foreign distributors (Esso and Shell) were nationalized and NOC became responsible for procurement and distribution of all petroleum products in Nepal. HMG became the majority shareholder, 98% (the original promoters had been Nepal Bank, National Trading Corporation, Rastriya Beema Sansthan and the Nepal Commercial Bank, which continue to hold the 2% balance). After some early years of profits and dividends, NOC began to report losses. One factor was the perceived need to invest in bulk storage facilities at various centers in Nepal, at the border transit point with India and at the port of Calcutta.

2. Operations

Around 1983/84 when NOC's profit picture was showing improvement, NOC began investigating the potential for lubricating oils. Initially planned as an internal activity, various private and public companies expressed interest and Nepal Lube Oil Ltd was established as a public limited company. It is now 53% owned by NOC, 27% by the interested companies and 15% by the general public through a recent SEC offering. HMG has no representation on the subsidiary's board of directors. A new corporation, Nepal Bitumen and Barrel Company, will be established to handle bulk bitumen, manufacture barrels and produce road emulsions. NOC will own 95% of this enterprise with the balance held by 15-16 public enterprises and private individuals. Shares may be floated on the SEC at some point in the future.

3. Current Status

With the recent liberalization of import licensing, technically NOC no longer has a monopoly on distribution of petroleum products. ut, as NOC freely admits, doubts about continuity of government policy are a deterrent to potential competitition. No one would want to replicate NOC's investment in bulk storage facilities only to lose their import licence at some subsequent time.

NOC's current turnover is in the area of Rs. 15-18 hundred million (+ or - $ 75 million). In each of the past two fiscal years, pretax profits have been well in excess of its Rs. 60 million paid-up capital (and have wiped out all accumulated losses). However, NOC is now seriously undercapitalized. Unsecured borrowings from commercial banks have reached levels as high as five times its paid-up capital, a violation of the 2:1 debt/equity provision of Nepal Company Law not to speak of sound financial management.

E. Rastriya Beema Sansthan

1. Background

Rastriya Beema Sansthan (NIC), the national insurance company, was founded in 1967 by HMG, Nepal Bank and the Central Bank to write life and general insurance. At that time there were perhaps one hundred branch offices of Indian insurance companies operating in Nepal, but following nationalization of the Indian insurance industry in 1973, the number dropped to two (one based in Bombay, the other in Calcutta). Nepal Bank also operates a subsidiary insurance business (traded on the SEC), primilarly for its own business activities. A new private insurance company that will offer both life and general is being organized and is expected to have a share offering in the near future.

2. Operations

NIC is and is not two separate companies. The term life operation is state-owned. The general insurance, principally casualty and fire, business has some 500 private shareholders resulting from an SEC offering. Ownership is as below:

	Life	General
Paid-up Capital:	Rs. 1.8 million	Rs. 8.2 million
Ownership:		
HMG	Rs. 0.5 million	Rs. 3.9 million
Central Bank	1.0	2.4
Nepal Bank	0.3	0.9
Private shareholders	-	1.0
	1.8 million	8.2 million

3. Current Status

According to management, general insurance is the most profitable business. The concept of life insurance is not well understood in Nepal. There are some 18,000 - 19,000 policy holders but the average value is relatively small.

NIC is one of the least-regulated companies it would be possible to find in any field anywhere. The sole legal restriction on life insurance operations, for example, is that 50% of premium income be invested in Nepal - a constraint perhaps for the remaining Indian insurors but clearly not for NIC.

CHAPTER V: STATUTORY CONSTRAINTS TO PRIVATIZATION

A. Legal Status of Public Enterprises

The basis for establishment and operation of public enterprises in Nepal rests in the 1962 Constitution, and more specifically Article 19 paragraph (3) which seeks "to establish a system that will provide maximum participation of the general public in the economic uplift of the country as well as encourage cooperative and private enterprise, and wherein no individual or class is able to exercise undue economic pressure upon another individual or class". The Constitution further sets forth among the nation's social and political objectives promoting the general welfare by establishing a society that is democratic, just, dynamic and free from exploitation by harmonizing the interests of different classes and professions.

Public enterprises in Nepal are legal entities possessing legal rights and duties which are to be exercised solely for the public good. Public enterprises, unlike normal private companies, are protected by the government. Their directors are not responsible for any loss or damage incurred in performance of official duties, nor may complaints or actions be brought against them in any court of law. Rules framed by public enterprises, in accordance with their enabling legislation and approved by the government, have the force of law.

Public enterprises do not function independently. All enabling acts contain clauses to the effect that the government shall from time to time give direction and it shall be the enterprise's duty to comply. The government's supervisory powers include the power of dissolution whenever deemed necessary and appropriate.

In furtherance of its constitutional objectives, the government has established public enterprises under more than a dozen general or specific statutes. The overall rationale appears to have been:

- industrial and commercial enterprises of a general nature and with access to capital are formed under the Company Act;

- enterprises with a more social or services orientation which may require HMG subsidies are formed under the Corporation Act;

- enterprises established as projects aided by foreign donors and with HMG support, control and supervision are formed under the Development Board Act; and,

- enterprises of a specific operating nature and of major social significance are formed under Special Acts.

The general statutes and the number of public enterprises established under each are*:

Company Act (36)
Corporation Act (6)
Development Board Act (3)
Commercial Bank Act (2)
Communications Corporation Act (4)

The public enterprises established by special statute (and the dates of their enactment) are the NIDC (1959), Employees Provident Fund (1962). National News Agency (1962), Gorkhapatra Corporation (1963), Royal Nepal Airlines (1963), Agriculture Development Bank (1967), National Insurance Corporation (1968), Guthi Sansthan (1976) and Nepal Electricity Authority (1984).

There are significant differences among the general statutes - and therefore among the enterprises created thereunder - in terms of the provisions for establishment, capital structure, functions, government control and dissolution. For example, the Company Act and Commercial Bank Act permit an enterprise to come into existence following approval by the relevant authorities while the Corporation Act, Development Board Act and Communications Corporation Act require formal notification in the official Gazette.

Under the Company Act, an enterprise must register its name, address and objectives together with a description of the share capital subscribed with, as appropriate, the Department of Industries or Department of Commerce. Under the Commercial Bank Act, an enterprise must first be approved by the Central Bank and thereafter comply with the provisions of the Company Act.

The Company Act, the Commercial Bank Act and four of the Special Acts (NIDC, NIC, Agriculture Development Bank and Nepal Electricity Authority) make provision for a General Assembly of Shareholders. The Communications Corporation Act and Gorkhapatra Corporation Act require that employees (who are alloted 25% of the share capital) be represented. The remainder contain no provision for constituting a General Assembly.

The Company Act confers broad powers to the General Assembly. The Communications Corporation Act and Gorkhapatra Corporation Act permit shareholders only the election of a single director and to deliberate on the enterprise's annual report.

As for the Board of Directors of a public enterprise, three - the Company Act, Commercial Bank Act and Nepal Electricity Authority - provide for representation in proportion to share ownership. The Corporation Act, Development Board Act, Employees Provident

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* See Appendix A for the enterprises currently in operation by administrative ministry.

Fund and Royal Nepal Airlines provide only for HMG nominees while the remainder prescribe a fixed number of directors irrespective of shareholdings.

The chief operating executive is generally nominated or appointed by the government from among permanent civil servants. The role and status of a CEO elected or appointed by a Board of Directors tends to be of somewhat lesser importance.

As well as appointing directors and managers, the government regulates conditions of employee service according to PSC regulations, exercises financial controls through prescribed borrowing procedures and periodic audits, and legal controls provided by the relevant enactment. The Company Act provides for the appointment of a liquidator and distribution of proceeds among creditors and shareholders. The Corporation Act and Development Board Act call for transfer of all assets and liabilities to the government while other acts are silent on the mechanics of dissolution.

The foregoing summary reflects a history of some 60 public enterprises having been established under fourteen separate laws over a period of more than 25 years. However, from the standpoint of prospective transfer to private ownership, the situation is far less complex.

This is quite simply because, of those enterprises which are the focus of this study, the vast majority have been formed under the Company Act. As may be seen in Appendix A, of the 25 SOEs administered by the Ministry of Industries, all but two (Butwal Spinning and NIDC) are Company Act entities. Five of the six SOEs which are assigned to the Ministry of Forestry and Soil were established under the Company Act as were three of the four under the Ministry of Supplies and Ministry of Commerce.

Thus, in all but a handful of instances, the enabling legislation which governs the productive public enterprises is that which would be controlling if they were in the private sector. As public enterprises at present, they obviously operate differently in terms of government directives, appointments and adherance to PSC regulations but, they function within the same legal framework that they would as private enterprises.

That is the good news. The bad news, as will be described immediately hereafter, is that the Company Act is by no means the only piece of legislation which governs the conduct of private sector companies in Nepal.

B. Regulation of Private Enterprises

There are perhaps 100 enactments which regulate or may affect some aspect of private company operations in Nepal. These range from the Constitution itself through the Company Act to specific laws covering import/export controls, foreign exchange, duties and taxation, patent and trademark protection, repatriation of capital, employment of foreign nationals, etc.

The problem, however, is not so much the number of laws as it is in their overlap. It is not safe to assume, for example, that if the Company Act does not proscribe, or is silent regarding a specific activity, that it is legally permissible. There may be one or more other acts, not by their titles seemingly relevant, which may bear on the permissibility of that activity.

The problem is compounded by three related factors. First, there are no official translations for a majority of these acts. In the absence of such, reference needs be made to the original test. Unofficial translations, particularly from non-HMG sources, can not be relied on. Second, the practice of law is not yet an established profession, at least in Western terms. There are approximately 1800 lawyers registered in the country of whom perhaps 200 are active - all as general practitioners. There are in Nepal no counterparts to the corporate lawyer who can be expected to have a working knowledge of all legislation bearing on the establishment and operations of a private company.

Finally, not all laws on the books are fully or uniformly enforced. Establishing a company's potential liability under such circumstances goes beyond what may reasonably be required of any lawyer, regardless of specialization.

Appendix C identifies, describes and analyzes in brief 40 acts which have been chosen as most important to a company's - including a divested SOE's - operation in Nepal. Included are enabling legislation for commercial banks, NIDC, SEC etc. which are relevant to a company's abilities to finance operations and raise capital.

The cut-off point for Appendix C was necessarily arbitrary. Appendix D lists a further 50 acts that were also subject to detailed review. For a given company there may be one or more laws in that listing which are at least as germane as any detailed in Appendix C.

Illustrative of the types of potential pitfalls to which private sector investors/owners/managers need be alert are the following.

- The Constitution itself provides that the PSC will exercise supervisory powers (the unofficial translation of civil service regulations exceeds 300 pages) over employees of any organization controlled by any public enterprise. This presumably applies to some of the companies whose shares have been underwritten and are currently traded on the SEC.

- HMG may control the production and distribution of any commodity deemed essential. However, implementation has been delegated to Zonal Commissioners and Chief District Officers whose ability to determine true supply/demand conditions is limited at best.

- The Foreign Exchange Control Act permits Nepalese with Central Bank approval to hold overseas bank accounts - which are prohibited under the Ban on Investment in Foreign Countries Act.

- Central Bank approval is required to establish, inter alia, finance companies - which has not been forthcoming although enabling legislation has been on the books for over two years.

- Under terms of the Income Tax Act (Section 19A), the Managing Director or Board of Directors are personally responsible for any taxes due following closure or dissolution of a company.

- Employment of foreign nationals is generally not permitted unless the Ministry of Labor determines that qualified Nepalese are not available.

- The Department of Taxation is bound by - but may not observe - exemptions granted under industrial incentive legislation, nor court rulings upholding such exemptions.

- Ineffective administration of the Land Revenue Act results in extended legal disputes regarding property titles.

- The 1973 Bonus Act requires any for-profit organization with 10 or more employees and Rs. 2 lakhs capital to distribute 10% of its annual profits as employee bonuses if it is in the private sector and 8% if in the public sector.

CHAPTER VI: FINANCIAL CONSTRAINTS

A. Securities Exchange Centre Ltd.

There have been at least two recent in-depth reports on SEC operations and responsibilities. Every effort will be made not to duplicate unnecessarily their findings and recommendations. In the context of this study, the SEC's importance rests on Chapter 2 (paragraph 3) of the Securities Exchange Act, 1983, which prohibits any individual or organization, other than the SEC and its authorized brokers, from dealing in any securities of any description.

Thus, the SEC is the sole source of, and medium for, primary and secondary capital market transactions in Nepal. Appendix E lists the 18 new issues that have been offered through the SEC. Of these, six were debentures; all but one (an Agriculture Development Bank floatation in fiscal 1984) were fully subscribed. Of the share issues (leaving aside the 1978 Balaju Yantra Shala offering as being too small to be indicative), investor response is summarized below:

Public Enterprises	Percentage Subscribed	Other Enterprises	Percentage Subscribed
Nepal Metal	2.7%	Nepal Battery	175.4%
Nepal Trading	4.3	Nabil Bank	263.0
Himal Cement	17.5	Nepal Indo Suez Bank	374.8
NIDC	23.0	Nepal Grindlays Bank	540.5
Hetauda Leather	40.4		
NIC	40.6		
Nepal Lube Oil	300.5		

In this context, it might be further noted that all three joint venture bank offerings limited the number of shares that could be purchased by any one subscriber (and had further restrictions as to voting rights). Only two - Nepal Lube Oil and NIC - of the public enterprise issues contained such limitations.

While generalizations based on a total of 18 issues over a 10 year period may be statistically questionable, it seems fair to conclude that Nepali investors are more comfortable with fixed income securities and with rare exception are least attracted by share offerings of public enterprises.

As well as being the sole source of new offerings, the SEC is also the only market maker. The situation here is a bit unusual in that while the Securities Exchange Act of 1983 mandates that all existing public limited companies list their shares with the SEC, the Securities Listing Regulation of 1984 requires that a company have at least 100 shareholders and, further, that at least 15% of the issued shares be owned by holders of 100 or less shares. Of the 12 issues that traded during fiscal 1987, only four met or came close to the 15% requirement. The SEC, thus, finds itself in the anomalous position of making a market in the shares of companies which by its own regulations are not qualified to trade.

Of greater concern in the context of this study is the extreme thinness of the market. Appendix F shows total trading activity for fiscal 1987 and for the first quarter of fiscal 1988. In the 1987 fiscal year, there were a total of 13,408 shares traded with a value of just over Rs. 8.1 million ($ 371,000). However, excluding Bishal Bazar (which is a special situation) and Bottlers Nepal (which may be), the value of the full year's trading was less than the equivalent of $ 86,000 - perhaps one thousandth of a fair day's volume on the NYSE.

B. Banking System

Of the five commercial banks, Nepal Bank has been in existence for 50 years, Rastriya Banijya for over 20 while the three joint ventures are of very recent origin. None have in-house investment/merchant banking expertise should HMG decide to seek advice in such areas. The joint venture banks can, of course, (as can the resident representative of Citibank) call on parent companies and affiliates. But that gives HMG no more assurance than a direct approach to any recognized investment firm in London, New York or Paris. Nepal Bank, by far the largest and most profitable, can by its charter underwrite the securities of public limited companies but has not chosen to do so. Its principal portfolio holding is shares of its own (also profitable) subsidiary, National Insurance & Transport Co. Ltd.

The Agriculture Development Bank's experience is almost totally that of a lender. NIDC has made a number of equity investments but has never really acted in the capacity of a promoter, deal-maker nor does it have the sort of general background necessary to issues of pricing and distribution.

While technically not part of the banking system, the Provident Fund Corporation is of significance in that it currently holds the equivalent of over $ 130 million from 280,000 depositors (primarily civil servants, teachers, police and military). Of the total, about $ 50 million is in fixed commercial bank deposits, $ 40 million is on loan to members, $ 35 million is in development bonds and the residual is invested in fixed assets, primarily commercial real estate. The corporation can invest in loans guaranteed by the government or government institutions (e.g. NIDC) but not in corporate shares or debentures, and appears to have no inclination to revise its charter to do so.

While much smaller, the NIC's financial situation is very similar. Policy premiums and reserves are invested primarily in tax-free development bonds and in commercial bank deposits. NIC is not prohibited from making share investments but has only rarely (e.g. Nepal Lube Oil Corporation) done so to date. NIC does not appear to be under any particular pressure either to maximize profits or build reserves.

C. Capital Market Development Fund

The Capital Market Development Fund was established in 1984 by agreement among the Central Bank, NIDC and the SEC. The initial capital was approximately $ 350,000 equivalent, subscribed 91%, 6% and 3% respectively by the three institutions. Underwriting commissions and interest income have brought the Fund's current resources to some $ 500,000 equivalent. The Fund is not bound by a formal charter or articles of association. Participation by commercial banks or other institutions such as NIC is possible and is said would be welcomed.

The Fund's objectives are to develop the capital market and provide underwriting support. To date portions of three new issues have been underwritten and commitments made for a fourth.

Broadening the Fund's resource base would certainly benefit the new issues market. But, if the Fund were to be involved in offerings of shares in public enterprises, other potential institutional participants could have problems with prospective conflicts of interest.

For example, one of the issues underwritten in part by the Fund was NIDC. Not only is NIDC a participant in the Fund, but it also owns 38% of the SEC's capital (while the Central Bank holds 36% and HMG the balance). NIDC owns shares in a number of other HMG enterprises, several of which NIDC would like to be able to sell. The SEC makes a secondary market in some of the issues NIDC holds as well as for the shares of NIDC itself. The extent of these interrelationships could leave other financial institutions hesitant in becoming too deeply involved in the Fund as now constituted.

D. Utility of Non-Traditional Mechanisms

There are a wide array of financial instruments, long established in other capital markets, which are not presently in use in Nepal. Among those that have been suggested as having possible application are equity-linked debentures and preference shares. However, in the context of this study, where the focus is privatization of public enterprises, consideration of these types of financial instruments raises two serious problems.

First is the general issue that for much of Nepal's present day populace, investing in any form of security is not a "traditional" activity. For generations, surplus income - as in many other countries - has gone into consumption, important ceremonies and/or tangible assets such as land and gold. In Nepal, moreover, there is a tendency to hold money simply in the form of currency (some studies have suggested as much as two thirds of total money supply). In terms of national economic development, it is certainly important that savings be redirected to more productive channels. But, if such efforts are to be successful, such channels will have to be perceived as offering safety, accessibility, liquidity and yield - the attributes of, initially, postal savings and commercial bank deposits followed in time by government bonds. These are not generally considered to be the characteristics of common shares, or of senior securities with equity features (generally in return for lower yields).

The second and totally unrelated problem is that securities such as convertible debentures and preference shares can not by definition facilitate the transfer of ownership necessary for privatization. The initial purchaser is buying a fixed income (or in the case of preferred stock, dividends if unearned are typically cumulative) security which at some future point in time may be financially rewarding to convert into the underlying equity.

There is one financial mechanism that does not now exist in Nepal that also could facilitate the process of privatization. It is the unit trust (mutual fund). In discussing the need for mobilization of Nepal's financial resources, the IFC has said of the unit trust concept:

> "If properly organized and managed, it could contribute significantly to the mobilization of resources and channel small savings for the development of the economy in general and of the corporate sector in particular. The need for such an institution in Nepal is justified on several grounds. It is a versatile institution and can through tailor-made schemes, suit different investment preferences, mobilize sizeable resources as it becomes established and potential investors become familiar with it. It can appeal to both the conservative and risk-taking investors. If successful, it can be a perennial and non-inflationary source of finance for development and can establish linkages with other financial institutions and join them in worthwhile development projects. In fact, it is an institution which can, without inhibition, provide resources for any viable economic activity provided such activity guarantees a reasonable return on its funds. It can offer effective competition to existing institutions in mobilizing savings through its efficient service, low cost operation, offer of risk-free instruments and attractive rates of return to investors and thus, by its example, could help improve the overall efficiency of the financial system. It essentially acts as a small saver's institution by mobilizing his savings, making a prudent selection of investments, and while assuring the safety of his investment, provides a steady return, a small appreciation and a possible

repurchase facility. It can, thus, insulate the investor against a variety of credit and liquidity risks. As prices for purchase and sale of units will be fixed at regular, periodic intervals, investors will be reassured when they buy or sell units. Trading can also take place on the SEC within the spread of buying and selling prices for units. Such an institution, therefore, can be a useful mechanism for broadening the capital market, an institution would be eminently suitable in an environment, such as in Nepal, where promoters are reluctant to offer their share capital to the public and the investing public is chary of investing in financial instruments.

The successful functioning of this institution will, of course, depend on how quickly it gets established, the avenues for investments available to it, patronage of HMG, suitable tax concessions and the quality and enterprise of its management. It may not be necessary for such an institution to invest only in industrial securities, which, in any case, may not be available in the quantities needed to satisfy its investment needs, even though these would have priority in its portfolio. The Trust could, therefore, be empowered to invest in any type of security provided the investment is sound, has a reasonable assurance of return of principal, and provides a sufficient return to meet its expenses and service the required yield to unit holders."

In, again, the privatization context, the Unit Trust has further merit. It would be a buyer of securities rather than simply a financial intermediary such as the SEC or Capital Market Development Fund. If share participation in privatized SOEs was under consideration, the Trust would have a fiduciary responsibility to its own holders not only in the selection of issues but also as to the price paid. On the one side, management would have to have the investment skills to determine whether a given security belonged in its portfolio. On the other, for that very reason the Trust's willingness - or lack thereof - to participate in any offering could provide market leadership. The Trust's leverage - to the benefit of the investing public at large - could prove pivotal: in requiring remedial actions before an issue was brought to market; in assuring full disclosure; in setting the timing, size and price; in subsequently monitoring the company's performance; and, in expanding the size and utility of the secondary market.

Last but not least, technical support from international organizations such as the World Bank and IFC to a new institution such as the Trust might be more available and more effective than piecemeal alternatives.

CHAPTER VII: POSSIBLE HMG CONSTRAINTS

A. Policy Posture

Given HMG's stated endorsement of privatization, it did not seem appropriate in official meetings to seek out - nor was there any intimation of - resistance to a policy of transfering public enterprises to private ownership. However, from informal discussions and from experience in other countries, there seem to be four areas which can be grouped under the general headings of possible policy concerns.

1. Sovereignty

   In the broadest sense, turning state enterprises over to the private sector can be seen as disposing of a nation's patrimony, of selling what belongs to all people to a certain few. In Nepal, moreover, many of the larger industrial enterprises were essentially gifts or grants to HMG from other sovereign nations.

2. Philosophical

   There are in many developing countries strongly held beliefs as to the need for state ownership of the means of production and/or for central planning as the preferred approach to economic development. Such views do not seem to be widely articulated in Nepal but, again, many HMG enterprises have been provided by the PRC or USSR where private enterprise has only recently been gaining some degree of respectability.

3. Bureaucratic

   In Nepal, as in many countries, public enterprises are grouped under specific line ministries, to whom they are responsible and from whom they receive direction, sometimes budgetary support and - all too often - surplus office holders. For senior officials in such ministries, privatization can threaten loss of prestige, power and patronage. Senior SOE managers also enjoy considerable prestige and, understandably, can feel threatened by the uncertainties inherent in privatization. One of the most able public enterprise CEOs was particularly disparaging of job opportunities offered by the private sector.

4. Labor Concerns

   This is probably the most endemic problem faced by governments contemplating divestitures. State enterprises tend, almost universally, to be overstaffed. A long-dormant SOE with little or no liklihood of reestablishing operation may nonetheless retain its work force. The situation becomes even more intractable in countries with strong trade unions or where labor unrest can threaten political stability. Even absent such conditions, surplus labor can present a serious obstacle to privatization. Labor laws in some countries can make termination of redundant workers prohibitively expensive if the full cost is to be borne by the new owners/managers. For government to absorb such costs in the form of a reduced selling price may be attacked as a "give-away" to vested interests.

B. Concentrations of Wealth

No government welcomes the prospect of transfering ownership of public enterprises to private interests already deemed to control an inordinate share of the nation's wealth. Yet, it is exactly those strata in the private sector that have the access to capital, the understanding of risk ventures and the ability to attract qualified management. They are most likely to make a privatized SOE a financial and economic success.

In Nepal, such concerns appear to have been reflected in the exceedingly cautious approach to past offerings of public enterprise equity. There have been no direct placements (though sale of Balaju Textile by advertised tender is supposedly under serious consideration), and sales through the SEC have been characterized by:

(1) the offering of a relatively minor percentage of the enterprises' equity; and,

(2) recently placed stringent limitations on the number of shares available to any single purchaser.

If, in the future, HMG does privatize 51% or more of a given SOE, (1) above will no longer serve as a constraint. If further, the secondary market develops as its supporters hope, the limits placed on initial share purchases will prove only a temporary restraint. Subsequent accumulations (even with shares in registered rather than bearer form) would be administratively very difficult to monitor or control. It is certainly beyond the capacity of the SEC with its multiple responsibilities and limited resources. It is also far too early to consider imposing statutory reporting requirements on the Nepali equivalent of "insider" trading. An interim measure might be to announce that a general monitoring responsibility had been assigned to, say, the Corporation Coordination Division in the Ministry of Finance.

The concentration of wealth issue is a legitimate concern, but it is only one facet: there are risks in taking control of a privatized SOE; the families in Nepal with established financial resources can best accept such risks; to the extent they do invest, that portion of their capital stays in the country; and, to the extent they are financially successful, both the economy and other smaller shareholders will benefit.

C. Implementation

After a divestiture policy has been promulgated there come the questions of (1) which enterprise/s to sell, (2) at what price and (3) how.

1. Which Enterprises?

To date in Nepal - as in many other countries - initial efforts have been to dispose of public enterprises which the government itself did not very much want. Not surprisingly, potential investors tended to share HMG's point of view. A somewhat different element in the problem may be seen in HMG's decision to make an offering of NIDC shares. NIDC is a development agency. By definition its foremost responsibility is not profit maximization; its loan and equity portfolio should include troubled companies. NIDC is not the sort of vehicle in which small investors should be encouraged to participate. Nor, as was the case with the Nepal Metal Company offering, should investors be invited to participate in the shares of a company fa. in advance of commercial operations - let alone demonstrated viability.

There are established public enterprises with proven operating and financial records. If privatization is to be meaningful, HMG must be prepared to give up control of such companies.

2. What Price?

The decision to put the shares of a successful company on the market is simply the first step. Equally important - but even more difficult - is determining a price that is fair to both seller and buyers. It is disturbing, though understandable, that the issue of price - and how it is arrived at - seems not to have been a subject of much informed deliberation in past offerings.

Part of the pricing dilemma may, again, reflect concern regarding relations with a donor country. SOEs of this nature frequently in retrospect appear to have been over capitalized (often with over capacity). The prospective writedown of assets and liabilities (together with attendant depreciation and financial charges) to reach a position of operating viability (and, therefore, saleability) could understandably give a recipient country some hesitancy. Such external factors aside, it is imperative to have a source/mechanism to help balance the legitimate goals of the seller, the buyer and any financial intermediaries that may be involved. At present, there are in Nepal - as described earlier - no resident organizations to which HMG can turn for advice and assistance. The SEC is not so equipped. The new joint venture commercial banks may in time develop merchant/investment banking capacities, but have not to date done so. There are certainly individuals in the business community with many of the requisite skills (as well as the necessary knowledge of Nepal), but whether one or more would be acceptable to HMG as unbiased advisors is, of course, unknown.

In the United States, underwriters of a company's first share offering would generally be more than satisfied to see the secondary market take the issue to a 10-15% premium over the prospectus price. The new owners have the opportunity of taking a reasonable reward for the risk of participating in an unseasoned issue while the selling shareholders have not been unduly penalized. In Nepal, receptivity to a new issue will almost certainly be based more on characteristics such as liquidity and yield than on the prospect for a quick windfall profit.

One question selling governments frequently face is whether to renovate the candidate enterprise in order to enhance its marketability/sales price. In the author's experience, a relevant analogy can be taken from the real estate market where modest sums devoted to essentially cosmetic improvements may be well spent but investments in major structural changes are seldom recouped.

3. How?

Implicit in the pricing process is a decision whether an enterprise is to be sold as a "going concern" or for its "break-up" value. For the latter approach to be successful, there needs to have been a finding, first, that net assets exceed liabilities (if not, a government's only realistic option is liquidation) and, second, that prospective buyers believe realizable net asset values exceed the government's asking price.

Sale as a going concern - with its anticipated future earnings and dividends - is intended to, and should, generate more revenue for a selling government than a straight sale of assets (but enterprises in the latter category may have represented greater drains on the central budget).

The author once had the unusual opportunity of planning and managing the first share issue in the history of a certain country. The identity of the country is irrelevant; its economic, social and physical characteristics are not. Infrastructure was well advanced, as was the financial system. Perhaps 95% of the populace were within an hour or less distance of a commercial bank office. Per capital income was relatively high as were propensities to save. Literacy (in one or both of the principal languages) was nearly universal. Academic/professional training in Europe was common - as, therefore, was exposure to sophisticated financial markets. It proved relatively simple to place preliminary offering notices in the local newspapers and thereafter to employ commercial bank branches as selling agents (for distribution of prospectuses, receipt of applications and collection of funds following final share allocations).

These conditions are not duplicated in Nepal. A very substantial percentage of the population can not, will not or should not participate in an SOE share offering. Once the decision has been made to bring a specific public enterprise to market, the commercial banks should be approached as to their willingness to act as agents or underwriters or both. Potential institutional investors - the banks, the NIC, a new Unit Trust - should be involved. It is very tempting to recommend that SOEs themselves be encouraged to participate as portfolio investors.

Finally, HMG should be prepared to consider sale of going concerns (as with asset sales) on the basis of direct negotiations, even advertised tenders, without share offerings. Even placement with a financial institution planning subsequent resale might be a possibility. These avenues may only be realistic in the case of smaller SOEs but, the options should not be foreclosed.

CHAPTER VIII: CONCLUSION AND RECOMMENDATIONS

A. Role of Public Enterprises

As described in the Introduction, the focus of this study has been on public enterprises in the productive sectors as opposed to those engaged in trading or service-oriented activities (where HMG has taken the lead in supply and distribution of essential commodities, foodstuffs, agricultural inputs).

In that context, state ownership is of relatively recent origin in Nepal. As of the mid 1950's the government had nationalized only one enterprise, the Nepal Bank. Further, the momentum for creation of public enterprises was relatively brief, peaking in the late 1960's, declining during the 1970's and virtually non-existent by the 1980's. Finally, Nepal is unusual in that so few of its producer SOEs result from economic nationalization or other takeovers of private sector concerns. The only company falling into that category, Raghupati Jute Mills, was essentially a salvage operation.

Towards the close of the 1970's, the government began making a distinction between "first generation" and "second generation" public enterprises. The former consisted of the older companies created during the initial four Plan periods (1956-74). These companies hold or share in virtual monopolies in productive sectors such as cement, textiles, sugar, leather products, cigarettes, pharmaceuticals, and petroleum products. They had for the most part been the creations of bilateral aid and in almost every instance became wholly owned by HMG.

The latter group is made up of enterprises approved during the fifth and sixth Plans (1975-84). The "second generation" designation refers not only to their later gestation but also to the fact that HMG (and/or SOE) ownership is generally less than total. As of the time of this study, not a single company in this group was understood to be in commercial production. While no detailed investigation has been attempted, nor would have been appropriate under the scope of work, it seems a reasonable guess that these enterprises will represent an aggregate net drain on the central budget into the 1990's. It may, therefore, be tempting for HMG to try to divest its position in some of the second generation companies (in fact, an unsuccessful effort was made to sell shares in Nepal Metal as long ago as 1979/80). There is certainly no intrinsic financial or economic reason for HMG not to seek divestiture; the major concern is that at least, over the near term, HMG consider avenues other than the share offerings which are better suited to the established "first generation" companies.

Finally, there is emerging what might be considered an unofficial "third generation" of public enterprises. It is this group that might most suitably be classified under that part of the scope of work which call for "identification, as many prove possible, of sectors where the government is contemplating further business expansions or diversifications and the external sources from which it may be seeking financing/technology therefor."

Expansions/diversifications are being contemplated but, except as noted below, they do not appear to be in response to any general or specific HMG policy initiative. What seems to be happening is that the more successful SOEs are identifying investment opportunities in fields other than their own and are using surplus retained earnings to exploit them. This has long been an approach favoured by the Salt Trading Corporation (while not an SOE, HMG has significant financial and economic interests). Now, some first generation SOEs are moving in the same direction and on occasion, employing foreign technical assistance in the new endeavors.

The author has no sense that the managers of these companies are in any way trying to subvert HMG privatization policies nor that personal gain is any particular objective. My impression is of very capable individuals who enjoy being SOE CEOs, but who also like the challenge of being involved with something new. Among the companies which have been mentioned earlier and which are beneficiaries of these SOE diversification activities have been Butwal Spinning, Nepal Lube Oil and Nepal Coal. Others are in formation or under consideration.

As to new activities with foreign involvement as formally endorsed by HMG, there is a possible new integrated textile mill which has been the subject of a recently completed Japanese feasibility study and, under currrent evaluation, possible equity and management inputs into one of the development finance companies (the PRC continues to assist in the construction of Butwal Spinning and Lumbini Sugar while, of course, the ADB has agreed to finance Nepal Paper).

Before leaving the subject of public enterprises, the author would like to return to the five specific SOEs described briefly in Chapter IV.

- BYS appears to be well managed and technically competent but has never been profitable because of its service and training orientation, self-induced competition (with lower overheads) and lack of proprietory product lines. It can stay as it is, or with the market orientation and incentives of a private for-profit company, try to really capitalize on its expertise.

- Butwal Spinning is a relatively rare instance in Nepal but frequent in other countries where profitable SOEs finance not only their own capital budgets but those of unrelated enterprises. Although trial production runs are not expected until 1989 at the earliest, the SEC is currently preparing a share offering prospectus which, on the basis of similar efforts in the past, will almost certainly be unsuccessful. A more productive approach might be a direct placement with a technically qualified private company or group.

- Janakpur Cigarette, a "turn-key" grant from the USSR had, until recently, a total monopoly on domestic production. It personifies the profitable public enterprise which governments find so difficult to relinquish. At the same time, there is every reason to believe that under private management freed from, inter alia, PSC regulations, productivity and profitability could be substantially increased.

- NOC is a very profitable company in serious need of an increased capital base. It has four long-term institutional shareholders that could well want to take up part of the new equity and, public response might be similar to the oversubscription of NOC's Nepal Lube Oil subsidiary. The one required ingredient would be that NOC be freed of administered pricing, but even an arrangement that permitted NOC to set product prices at, say, cost plus 5% would result in a highly viable company.

- RBS is profitable, unregulated and operates with virtually no internal guidelines. Policy premiums are based on "tariffs set long ago in India"; the company has no actuarial competence or standards. There is even question as to whether the general insurance operation with its private shareholders may be subject to potential liabilities from life insurance claimants. With a new private insurance company in formation, it might be opportune to discuss some form of amalgamation.

B. Obstacles to Privatization

To oversimplify a bit for emphasis, the obstacles to privatization in Nepal are not statutory, philosophical or political. They are essentially practical reflections of inherent caution, inexperience and government-to-government relations. As discussed in Chapter V, there are no laws, statutes, enactments on the books that would require amendment to permit privatization of the vast majority of productive SOEs in Nepal. There is need for a rigorous review of the rules governing conduct of private businesses, but that is another matter. Any of HMG's public enterprises established under the Company Act can be privatized without legal constraint.

In terms of new legislation which could clarify the private sector's rights and role in Nepal, HMG might consider the following.

- Separate laws for public enterprises, private companies and banking companies. At present HMG appears to assume that all three operate under the same norms and standards.

- Specific legislation setting forth the powers, limits and remedies available in the event of any future nationalization. At present HMG may take over any venture on any pretext.

- A "Privatization Statute" describing incentives and concessions which might be offered to potential investors (analogous to locational tax holidays offered by Nepal and many other countries).

- Legislation establishing HMG's obligations to employees made redundant by liquidation or privatization of public enterprises. In the past HMG has simply compelled other SOEs to absorb such workers (Ref: B.S. Karki Vs. Nepal Food Corporation, Supreme Court 1105 of 1983).

- Changes in policy are not necessarily reflected in corresponding changes in law; changes in law are made which reflect no apparent changes in policy. A current statement of what constitutes the public sector domain and boundaries might begin to build private sector confidence.

In terms of philosophical and political constraints, HMG does not face, at least relative to many other countries attempting privatization, issues/forces such as:

- accusations of "turning back the clock" to pre-independence or colonial periods;

- rationalizing the return of nationalized sectors or industries to private initiative;

- the exceedingly complex compensation questions when companies are to be reacquired by their previous owners;

- organized and articulate intelligentsia committed to state ownership/central planning;

- entrenched trade unionism; or

- severe ethnic divisions which make transfer to certain groups politically unpalatable.

In other words, there seems little reason for HMG to be on the defensive, philosophically or politically, when it comes to privatization. The areas under consideration are the productive sectors, wherein there is virtually world wide acceptance that government functions least effectively. The enterprises under consideration will, for the most part, be older factories built with bilateral financial and technical assistance. Increased efficiencies, whether in terms of capacity utilization, productivity or economic self-sufficiency, are stated government objectives; privatization is the only apparent means to such ends.

C. Facilitating Privatization

In a perfect world, the next step toward facilitating privatization in Nepal would be for HMG, perhaps as a part of the forthcoming 7th Plan mid-term review, to publish a consolidated statement setting forth its objectives, strategy, program, schedule, and implementing authority. Even accepting the realities of an imperfect world, HMG needs to reach beyond the hesitant, piecemeal and uncoordinated approaches that have been characteristic of efforts to date. It cannot be overemphasized that the private sector - the prospective buyers - need assurance that HMG is proceeding on the basis of some reasonably coherent plan.

Those are prerequisites for successful broadscale privatization. To achieve them, HMG needs access to respected investment/merchant banking know-how. Such expertise does not - in any institutional sense - exist in Nepal, nor is it likely to develop over the near future. As touched on earlier, the necessary experience runs the gamut from company accounting and analysis ("going concern" versus "break-up" evaluation) to pricing and sale (share offering, direct placement, merger, acquisition).

In Chapter III, reference was made to HMG's current preference for a public enterprise negative list, i.e. sectors and companies that would remain in the government domain. While that is apparently acceptable to the World Bank, it would nonetheless be a very constructive step if HMG were to formally announce an initial listing (it can be as short as one name) of privatization candidates. This should not however be done until and unless HMG is irrevocably committed to sale of each enterprise so identified - the list can always be increased but to remove a name would be at severe cost to HMG's credibility. Doing so will not only establish the "who", but in practice will also help determine the "what price" and "how" (discussed in the preceding chapter).

To go off on a brief but necessary tangent, the scope of work calls for a preliminary investigation of the private sector's receptivity/capacity to absorb non-traditional financial instruments and to provide preliminary conclusions. From the limited evidence available, there would definitely seem to be a potential for corporate debentures from private companies with name recognition (e.g., Bottlers Nepal). Such debentures probably can be unsecured, but in the early stages may have to be offered on terms (yield, maturity) that do not provide the issuing company significant savings over the costs of commercial bank borrowings. The author also feels that the inclusion of conversion privileges or other equity-linking features would at this stage materially reduce the price at which public limited companies could successfully sell debenture issues.

As noted earlier, whether or not there is a market for such issues is essentially irrelevant in the context of privatization. The unit trust, as discussed in Chapter VI, is relevant. Further, if the concentrations of wealth issue is a matter of serious concern within HMG, the unit trust again has attraction in that its holders have no direct access to the operating companies in which the trust invests.

If the unit trust concept proves to have appeal there are at least two immediate questions that should be raised with HMG. One is providing tax exemption on trust dividends, at least for some period of years. The second is whether the trust could qualify among those financial institutions permitted to buy and hold national savings bonds. Both questions relate to the trust's presumed need to be able to offer financial returns that are reasonably competitive with alternative investment vehicles.

In terms of immediate priorities, the two uppermost are for HMG:

- to define conclusively a "short list" of SOE's to be sold. All enterprises so included should have name recognition, records of successful operations, established positions in growing sectors of the economy and lend themselves to divestiture through share market offerings; and,

- to establish one or more qualified sources of technical assistance in determining the sequence, timing, pricing, market mechanisms, etc., to effect such transfers.

Of virtually equal priority is an official announcement that henceforth HMG will relinquish ownership, board and management control of any enterprise formally designated for privatization and where specific circumstances dictate also abolish indirect controls such as administered pricing.

Next, assuming timely provision of technical assistance, would be to settle on the order in which, say, the first three or four SOE's are to be sold, the amounts to be offered and (perhaps in consultation with the local banking community) the timing.

During the same period, HMG should seek World Bank/IFC assistance in forming a unit trust and in deciding what financial incentives might be made available to it and/or its holders. A decision could be taken as to whether to relieve the SEC of responsibility for monitoring the secondary share market and, if so, whether the Corporation Coordination Division is best suited to take on that function. Attention should also be given to rationalizing the overlapping and conflicatory enactments affecting the environment in which the private sector operates.

Thereafter, with the requisite technical assistance in place and six months a reasonable expectation, a selected HMG public enterprise could be nearing readiness for market. But, first steps first: HMG needs to be unconditionally committed to, and have the skills available for, the entire privatization process.

APPENDICES

APPENDIX - A

(51-100% Gov't Ownership)

	Sector	Chief Executive Officer	Phone (Kath)	Address	Mode of Creation and (Date of Establishment)	Principal Activity	No of Employees	Market Share	Ownership Pattern GON	Foreign	SOE	Private	1985/86 Profit (Loss) in '000	Pricing Pattern	External Aid
A. MINISTRY OF AGRICULTURE															
1. *Agriculture Development Bank	Financial	Shri Krishna Upadhya	213819	Kathmandu	Ag Dev Bank Act, (1968)	Provide loans for agricultural development & to supply ag inputs on credit	3408		80.8%		12.0%	7.2%	73 A)	-	
2. *Ag Inputs Corporation	Trade	Dr Kamala Bhakta Rajbhandari	212507	Kathmandu	Corporation Act, (1974)	Procure & distribute ag inputs to farmers at reasonable prices	1023	100%	100%				(475)A)	Subsidy	
3. *Agriculture Tools Factory	Industrial	Amar Bahadur Karki	412188	Birgunj	Company Act, (1969)	Design, manufacture and market improved varieties of agricultural inputs	263		100%				(27)A)	Autonomy	USSR
4. *Agro Lime Industry	Industrial	Ganesh Bahadur Bhusgare	215458	Chobhar	Company Act, (1974)	Produce agricultural & chemical lime	75		100%				(7)A)	Autonomy	
5. *Dairy Development Corp	Industrial	Dr Durga Datta Joshi	414841	Kathmandu	Corporation Act, (1969)	Collect, process, preserve & supply 60,000 liters of milk per day through its four centers in Hetauda, Kathmandu, Biratnagar & Pokhara	1200	67%	100%				(54)A)	Autonomy	
6. *Nepal Tea Dev Corporation	Industrial	Rohit Bahadur Thapa	215422	Jhapa	Company Act, (1967)	Produce tea for domestic consumption & export	333	14%	100%				(63)A)	Autonomy	
B. MINISTRY OF INDUSTRY															
7. *Balaju Textile Industries	Industrial	Thakur Bahadur Karki	413958	Kathmandu	Company Act, (1972)	Manufacture textiles from woolen, cotton and synthetic yarns	290	1%	79%		21%		(131C)	Autonomy	
8. Balaju Yantra Shala (P) Ltd	Industrial	Shridhar Bevkota	412379	Kathmandu	Company Act, (1960)	Steel fabrications	120	15-20%		85%	15%				Swiss
9. Balaju Yantra Shala Sanitary Engineering Ltd	Industrial		410840	Kathmandu	Company Act	Plumbing				35.55%	62.37%	2.08%			Swiss
10. *Bansbari Leather and Shoe Factory	Industrial	Ajit Narayan Singh Thapa	414561	Kathmandu	Company Act, (1965)	Produce 300 pair of shoes & 300 cu.ft. of tanned leather a day	378	26%	100%				20 C)	Autonomy	China
11. *Bhaktapur Brick Factory	Industrial	Rameshwore Prasad Shah	215211	Bhaktapur	Company Act, (1975)	Production of 100 million bricks annually	470	3%	100%				(7)C)	Autonomy	China
12. *Bhrikuti Paper Factory	Industrial	Prakash Mani Ghimire	522305	Nawalparasi	Company Act, (1982)	Produce 3000 M.T. of paper per year	127	15%	100%						China
13. *Birgunj Sugar Factory	Industrial	Durga Prasad Pandey	214664	Birgunj	Company Act, (1964)	Produce 15000 M.T. of sugar a year	1552	38%	100%				101 C)	Monopoly	USSR
14. Butwal Spinning Mill	Industrial	Bhava Sagar Sharma	413789	Butwal	Corporation Act, (1983)	Production of 2745 M.T. of yarn/year	660		1.9%		62.4%	35.8%			China
15. *Cottage Industry and Handicraft Emporium	Trade	Swarna Bikram Thapa	214290	Kathmandu	Company Act, (1966)	Buy & sell products produced by domestic small industries	229						19 C)	Autonomy	
16. Gorakhkali Rubber Plant	Industrial			Gorkha	Company Act	Produce trucks & jeep tyres	1000	60%	12.75%		40%	47.25%			China
17. *Harisiddhi Brick & Tile Factory	Industrial	Jagadish Prasad Sharma	521451	Harisiddhi	Company Act, (1970)	Manufacture 132 million bricks plus roof and floor tiles	578	8%	100%				6 C)	Autonomy	China
18 *Hetauda Cement Factory	Industrial	Rabindra Rimal	410145	Hetauda	Company Act, (1976)	Manufacture 700 M.T. of portland cement a day	1100	50%	100%				(722)C)	Autonomy	ADB

	Sector	Chief Executive Officer	Phone (Kath)	Address	Mode of Creation and (Date of Establishment)	Principal Activity	No of Employees	Market Share	Ownership Pattern GON	Foreign	SOE	Private	1985/86 Profit (Loss) in '000	Pricing Pattern	External Aid
19 *Hetauda Textile Industry	Industrial	Keshab Prasad Pradhan	410932	Hetauda	Company Act, (1974)	Manufacture 1 million meters of cotton textiles	1276	4%	100%				6 C)	Autonomy	China
20 *Hetauda Cement Company	Industrial	Indra Bahadur Shah,	212763	Chobhar	Company Act, (1970)	Manufacture 180 M.T. (to be 400 M.T.) of portland cement per year	711	25%			95%	5%	23 C)	Aut[illegible]	FRG
21 Integrated Textile	Industrial			Rapati	Company Act	Manufacture textiles			100%						Japan
22 *Janakpur Cigarette Factory	Industrial	Devendra Bahadur Shah	221238	Janakpur	Company Act, (1965)	Produce 500 million cigarettes per month	2713	99%	100%				413 C)	Autonomy	USSR
23 Lumbini Sugar Factory	Industrial	Kalyan Bahadur Pradhan	522315	Nawalparasi	Company Act, (1982)	Produce 10,000 M.T. of sugar/year	650-1000	25%	100%						China
24. *Nepal Industrial Development Corporation	Financial	Ramesh Nath Dhungel	411322	Kathmandu	Nepal Industrial Dev Corporation Act, (1959)	Provide loans and equity to private enterprises	313		98.4%			1.6%	13 C)	Subsidy	
25. Nepalgunj Paper Industry	Industrial	Binod Bistha		Nepalgunj	Company Act, (1983)	Produce 9,900 M.T. of printing & writing paper per year	536	56%	100%						ADB
26 *Pashupati Jute Mills	Industrial	Keshab Prasad Sharma	214625	Biratnagar	Company Act, (1960)	Procure & process jute	2501	46%			65.1%	34.9%	(285)C)	Autonomy	ADB
27 *Security Exchange Center	Financial	Baburam Prasad Dhungel	411031	Kathmandu	Company Act, (1976)	Promote industrial entrepreneurship on the legal set up of public limited companies	33	100%	26%		74%		13	-	
28 Seti Cigarette Factory	Industrial			Dhangadi	Company Act	Produce 650 million cigarettes per year	600				51%	49%		Autonomy	
29. The Hides and Skins Corporation	Industrial				Company Act	Produce 240,000 pieces of leather per year					58.1%	41.9%			
30 *Tobacco Dev Company Ltd	Trade	Pradyuman Lal Karna		Janakpur	Company Act, (1971)	Encourage tobacco cultivation	886						(8)C)	Monopoly	
31. Udayapur Cement Factory	Industrial	Lava Kumar Devkota		Udaypur	Company Act	Produce 800 M.T. of cement a year			100%						Japan
C. MINISTRY OF FINANCE															
32 *Credit Guarantee Corporation	Financial	Bijaya Ram Mathema	413659	Kathmandu	Company Act, (1974)	Guarantee loans made by commercial banks to priority sector industry, agriculture & service sectors	21		49.30%		50.7%		15 A)	-	
33. Nepal Bank Limited	Financial	Ananda Bhakta Rajbhandari	221337	Kathmandu	Commercial Bank Act, (1937)	Mobilize savings & channel for the development of trade & industry	8060	65%	51.8%			48.2%		-	
34. Provident Fund Corporation	Financial	Tek Bahadur Khatri	224928	Kathmandu	Provident Fund Act, (1961)	Collect & safeguard the provident fund of employees of HMG & other public & private sector bodies	600					100%		-	
35 *Rastriya Banijya Bank	Financial	Laxman Bahadur Hamal	410852	Kathmandu	Commercial Bank Act, (1964)	Mobilize capital resources & channel for development of trade & industry	5752		100%				(11A)	-	
36 *Rastriya Beema Sansthan	Insurance	Hara Pratap K.C.	213882	Kathmandu	National Insurance Corp Act, (1968)	Underwrite life & general insurance	200	Life	27.8%		72.2%		622 A)	Autonomy	
								Several	47.8%		40.4%	11.8%			

	Sector	Chief Executive Officer	Phone (Kath)	Address	Mode of Creation and (Date of Establishment)	Principal Activity	No of Employees	Market Share	Ownership Pattern GON	Foreign	SOE	Private	1985/86 Profit (Loss) in '000	Pricing Pattern	External Aid
D. MINISTRY OF FOREST & SOIL CONSERVATION															
37. *Fuel(wood) Corporation	Trade	Semanta Prasad Regmi	413367	Kathmandu	Corporation Act,(1965)	Sell & distribute fuelwood at fair prices & to conserve the the country's forest resources	443	60%	100%				84 A)		
38. Herb Production & Processing Ltd	Industrial	Dr Asfaq Sheikh	413942	Kathmandu	Company Act,(1978)	Production of herbal medicines	110		70%		10%	20%	(22)C)	Autonomy	
39. *Royal Drugs Ltd	Industrial	Madan Das Tuladhar	221512	Kathmandu	Company Act,(1972)	Increase domestic drug production	500	12%	100%				35 A)	Autonomy	
40. Rosin and Turpentine Company	Industrial		413299	Dandeldhura	Company Act,(1982)				100%						USSR
41. *The Timber Corporation of Nepal	Trade	Santosh Bikram Shah	212192	Hetauda	Company Act,(1960)	Process timber and undertake sale, & import of timber & timber products	1224		100%				41 A)	Autonomy	
E. MINISTRY OF COMMUNICATION															
42. *Gorkhapatra Corporation	Utilities	Nagendra Sharma	213902	Kathmandu	Gorkhapatra Corp Act,(1963)	Provide information on national & international events through the publication & distribution of papers	660		100%				8 A)	Monopoly	
43. *Nepal Tele-communication Corporation	Utilities	Suresh Kumar Pudasaini	215444	Kathmandu	Communication Corp Act,(1959)	Provide economic and efficient tele-communication services	2975	100%	100%				406 A)	Monopoly	
44. *Nepal Television	Utilities	Nir Bikram Shah	215000	Kathmandu	Communication Corp Act,(1985)	Provide information on national & international events	101	100%	100%				(25)A)	-	
45. *Ratna Recording Corporation	Utilities	Shiva Shankar Manandhar	214548	Kathmandu	Communication Corp Act,(1962)	Produce discs for tourism,education & to develop the market for Nepalese music	37	100%	100%				(7)A)	Subsidy	
46. *Royal Nepal Film Corporation	Utilities	Teeka Singh	411819	Kathmandu	Communication Corp Act,(1971)	Communicate national art to the people	98		100%				(37)A)	Autonomy	
F. MINISTRY OF COMMERCE															
47. *Jute Development and Trading Corporation	Trade	Laxmi Lal Shrestha		Biratnagar	Corporation Act,(1974)	Help increase the production of jute & regulate internal & external trade	216		100%				(835)A)	Subsidy	
48. *National Trading Limited	Trade	Sher Bahadur Pandey	212924	Kathmandu	Company Act,(1962)	Diversify foreign trade, regularize the supply of basic consumer goods & engage in trade under bilateral agreement	763		100%				5 A)	Autonomy	
49. Nepal Coal Ltd	Trade	Pashupati Pratap Shah		Kathmandu	Company Act,(1985)	Import and distribute coal		100%			100%				
50. *Nepal Transit & Warehousing (P) Ltd	Utilities	Shantaram Bhandari	211551	Kathmandu	Company Act,(1971)	Provide transit facilities for foreign trade	138		100%				2 A)	Autonomy	

	Sector	Chief Executive Officer	Phone (Kath)	Address	Mode of Creation and (Date of Establishment)	Principal Activity	No of Employees	Market Share	Ownership Pattern GON	Foreign	SOE	Private	1985/86 Profit (Loss) in '000	Pricing Pattern
G. MINISTRY OF EDUCATION														
51. *Cultural Corporation	Social	Ganesh Rasik Rai Guruacharya		Kathmandu	Communication Corp Act,(1972)	Organize & conduct cultural events	111	100%	100%				(71A)	Subsidy
52. *Janak Educational Materials Center Ltd	Utilities	Bishwo Nath Adhikari	214785	Sano Thimi	Communication Corp Act,(1978)	Prepare, develop, publish & sell educational materials at fair prices	515		100%				54 A)	Monopoly
H. MINISTRY OF SUPPLIES														
53. *Nepal Food Corporation	Trade	Ram Prasad Joshi	214773	Kathmandu	Corporation Act,(1974)	Procure,distribute & sell food grains at concessional prices in food deficit and remote areas	1149	26%	100%				(12051A)	Subsidy
54. *Nepal Oil Corporation Ltd	Trade	Guna Raj Upadhya	214970	Kathmandu	Company Act,(1971)	Import and distribution of petroleum and petroleum products	497		99%		2%		650 A)	Monopoly
55. Nepal Lube Oil	Trade	Madan Raj Sharma		Amlethgunj	Company Act,(1985)	Blend & sell 5000 M.T. of lubricants a year		100%			80.98%	19.02%		
56. Nepal Bitumen & Barrel Industry	Industrial			Amlethgunj	Company Act	Manufacture barrels & produce road emulsions					95%	5%		
I. MINISTRY OF WATER RESOURCES														
57. *Drinking Water & Sewerage Corporation	Utilities	Surendra Bahadur Shrestha		Kathmandu	Dev Board Act,(1973)	Develop drinking water supply & sewerage system	1456	100%	100%				(3021A)	Monopoly
58. *Nepal Electricity Authority	Utilities	Harsha Man Shrestha	212952	Kathmandu	Electricity Authority Act,(1985)	Distribute electricity	6700	100%	100%				281 A)	Monopoly
J. MINISTRY OF WORKS AND TRANSPORT														
59. *National Construction Company of Nepal	Utilities	Dr Ratna Lal Shrestha	212226	Kathmandu	Company Act,(1961)	Plan, design & construct civil engineering projects	373		100%				(71B)	Autonomy
60. *Transport Corporation of Nepal	Utilities	Tirtha Bahadur Pradhan	214797	Kathmandu	Corporation Act,(1965)	Regulate and operate public means of transportation viz. railway,ropeway, bus and trucks services	1063		100%				(341A)	Autonomy
K. MINISTRY OF TOURISM														
61. *Royal Nepal Airlines Corporation	Utilities	Bali Ram Singh	231513	Kathmandu	RNAC Act,(1962)	Manage air transport services	2130	100%	100%				387 A)	Monopoly

M.T. = Metric Tons
A) Gross Operating Profit (Loss)
B) Pre-Tax Profit (Loss)
C) After-Tax Profit (Loss)

* Government enterprises listed in the "Progress Report and Targets of Government Corporations for FY 1986/87 and FY 1987/88", published by the Ministry of Finance.

Appendix B

INDUSTRIES WITH 50% OR LESS GOVERNMENT OWNERSHIP*

Name of Industry		Ownership
1.	Biratnagar Jute Mills Ltd.	HMG 12.45%, Private 87.55%
2.	Bishal Bazar Co. Ltd.	SOE 34.13%, Private 65.87%
3.	Butwal Power Company	NIDC 29%, NEA 2%, UMN 69%
4.	Dhankuta Cold Storage (P) Ltd.	NIDC 98%, Sajha 2%
5.	Housing Management Company	Himal Cement 28%, Private 72%
6.	Hetauda Leather Factory	SOE 28.73%, Private 71.27%
7.	Hetauda Flour Mill	STC 95%, NTL 5%
8.	Kathmandu Bread Factory	SOE 49.58%, Private 50.4%
9.	Morang Sugar Mills	HMG 0.22%, Private 99.78%
10.	Nepal Arab Bank Ltd.	SOE 16.08%, Foreign 52.45%, Private 31.47%
11.	Nepal Cigarette Factory	HMG 13%, Private 87%
12.	Nepal Indo Suez Bank Ltd.	SOE 45%, Foreign 50%, Private 5%
13.	Nepal Insurance and Transport Co.	Nepal Bank 50.97%, Private 49.03%
14.	Nepal Grindlays Bank Ltd.	SOE 35%, Foreign 50%, Private 15%
15.	Nepal Metal Company	HMG 50%, Hong Kong 25%, India 25%
16.	Nepal Orind & Magnesite Co.	HMG 50%, India 25%, Private 25%
17.	Pokhara Bread Factory	SOE 50%, Private 50%
18.	Salt Trading Limited	HMG 10%, NTL 15%, Private 75%
19.	Soaltee Hotel	SOE 31.54%, Private 68.46%
20.	Sunsari Sugar (under consideration)	STC 51%, Public 49%
21.	The Juddha Match Factory (Biratnagar)	HMG 0.14%, Private 99.86%
22.	Yak and Yeti Hotel	SOE 17.48%, Private 82.52%

NEA = Nepal Electricity Authority
NIDC = Nepal Industrial Development Corporation
NTL = National Trading Limited
SOE = State Owned Enterprises
STC = Salt Trading Corporation
UMN = United Mission to Nepal

* List is incomplete.

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Appendix C

LIST OF LAWS AND REGULATIONS GOVERNING PRIVATE ENTERPRISES IN NEPAL

Summarized

1. The Constitution of Nepal 1962
2. Conduct of Essential Services Act 1957
3. Essential Goods Protection Act 1965
4. Essential Commodities Act 1959
5. Foreign Exchange Control Act 1962
6. Foreign Exchange Regulation 1963
7. Loan and Guarantee Act 1968
8. Export Import Control Act 1955
9. Export Import Rules 1977
10. Nepal Rastra Bank Act 1955
11. Commercial Banks Act 1974
12. Finance Company Act 1985
13. Company Act 1964
14. Private Firms Registration Act 1956
15. Private Firm Registration Rules 1977
16. Industrial Enterprises Act 1981
17. Partnership Act 1962
18. Foreign Investment and Technology Act 1981
19. Securities Exchange Act 1983
20. Securities Exchange Listing Regulation 1983
21. Nepal Industrial Development Corporation Act 1959
22. Income Tax Act 1974
23. Income Tax Rules 1966
24. Sales Tax Act 1966
25. Sales Tax Rules 1967
26. Customs Duties Act 1962
27. Customs Duties Rules 1970
28. Excise Duties Act 1958
29. Excise Duties Rules 1962
30. Provisional Taxes Collection Act 1954
31. Contract Tax Act 1966
32. Contract Tax Rules 1966
33. Acquisition of Lands Act 1977
34. Requisition of Immovable Property Act 1956
35. Land Revenue Act 1976
36. Land Revenue Rules 1980
37. Nepal Factory and Factory Workers Act 1959
38. Nepal Factory and Factory Workers Rules 1963
39. Bonus Act 1973
40. Bonus Rules 1982
41. Lands Act 1964

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	Title	Date of Promulgation	Year Amended	Activities Affected	Executing Authority
1.	The Constitution of Nepal	1962	1967 1975 1980	All citizens shall have freedom to acquire and enjoy property or to dispose it of by sale or otherwise (including freedom to operate any business or profession). No person shall be deprived of his property save in accordance with the law. The State is constitutionally bound to ensure maximum possible participation of the general public in the economy of the country, provide appropriate protection to private enterprise and establish a syst m of cooperative societies as the basic foundation of the industrial and commercial policy of Nepal. The Public Service Commission shall be consulted in the making of rules concerning the conditions of service of the employees of the government owned or controlled corporate bodies or of the organisations owned or controlled by such corporate bodies. The Public Service Commission shall exercise a supervisory control to ensure that these rules and the general principles have been complied with [Article 78 (3A)].	His Majesty the King. Rights guaranteed; cannot be abridged by legislative enactment or statute. Directive, principles are only for generaly guidance and are not enforceable by any court.

A. Summary of Objectives

The Constitution provides certain guaranteed fundamental principles to give recognition to and ensure protection from arbitrary encroachment of the state. The state is directed to observe and follow such policies while implementing each and every economic development program. Recognition of "private enterprise" and "private property" in the constitution is emphatically clear.

B. Current Constraints

Although recognition of "private enterprise or the private sector" is legally established in practice, there has been no consistent policy approach. The common principles as laid down by the PSC as binding on all public enterprises necessarily limits the autonomous character of these enterprises.

C. Possible Improvements

Mere declaration of principles in the constitution has not proved sufficient. Frequent changes in industrial and commercial policy have inhibited the meaningful development and expansion of the private sector in Nepal.

2.	Conduct of Essential Services	1975		To maintain an uninterrupted supply of essential services. HMG is empowered to declare and take control of postal services, telephone and telecommunications services, transport, etc., as essential services. Strikes by employees of such services may be declared illegal. Provision for penalties.	HMG to execute the law
3.	Essential Goods Protection Act	1955	1960 1962 1965 1974 1976 1981	Certain essential goods such as telegraph, telephone, ropeway, highway, drainage etc. are defined as essential goods. Disruption or destruction is punishable.	HMG to determine the list of essential goods, Zonal Commissioner to punish violations.

A. Summary of Objectives

The purpose of these two enactments was to empower HMG to use certain extraordinary powers to maintain regular supplies of and protect essential services/goods.

B. Current Constraints

The power delegated to HMG by these enactments is vast. Some of the services might be performed better with private sector participation.

4.	Essential Commodities Control Act	1959	1961 1972	Essential Commodities as defined include almost all types of commodities in daily use. HMG may take control of production and distribution of essential commodities at	HMG may issue orders to execute the law.

any time to increase distribution, maintain supply or to insure equitable distribution at fair prices.

HMG empowered to regulate, control and restrict production, distribution and movement of essential commodities if considered in the public interest.

Provision for penalty for non-observance of HMG orders.

Provision for delegation of authority.

A. Summary of Objectives

With a view to maintaining a regular and adequate supply of goods needed on a daily basis, HMG has been entrusted with sweeping powers.

B. Current Constraints

HMG has made it a practice to delegate most of the powers vested in it to Zonal Commissioners and Chief District Officers almost without control. These authorities are responsible by and large for maintaining law and order and, as such, may have no means of collecting information about the supply and demand of essential goods. Application of these powers tends to be arbitrary. There is overlap between this act and other legislation which creates additional problems.

C. Possible Improvements

The laws should be amended and probably consolidated into a single Act. To insure purposive implementation, a competent authority should be responsible for its implementation based on an adequate market information system.

5.	Foreign Exchange Control Act	1962	1963 1987	Exchange of any foreign currencies by or with any one not holding a duly authorized exchange permit is illegal and punishable. Foreign exchange permits are issued by NRB on application from interested persons (not free for all). HMG may require anyone holding foreign exchange to deposit same with the bank or anyone authorised by it.	HMG may frame rules in consultation with NRB and may issue directives. Specified court to hear appeals.

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			Export or import of bullion and currency may be restricted and NRB may impose restrictions on sale, purchase or dealings.	
			HMG may prohibit exports of any goods or commodities until satisfied that payments would be made in acceptable foreign currency.	
			Export and transfer of securities subject to permission from NRB.	
			NRB may require owners of foreign exchange to submit statements regarding their holdings.	
			No contract can be entered into or concluded in contravention of this Act; if done, it may be declared null and void by order of the concerned court.	
			HMG or NRB authorised to effect inspection of any person or place suspected of violating the law.	
			Nepalese nationals require NRB's permission to open and operate accounts in a foreign bank (this is in direct contravention of the Investment in Foreign Countries Act which prohibits such Acts.	
6.	Foreign Exchange Regulation Control Rule	1963	Certain purposes specified for which NRB could grant a foreign exchange facility.	HMG to control and regulate foreign exchange.
			Among others, NRB to provide foreign exchange for businessmen to travel abroad.	NRB to execute control and issue regulations concerning foreign exchange.

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				Exporters exporting under license are required to submit statements and records/documents to substantiate payments in foreign currencies. Importers with duly granted import licenses to be provided with necessary foreign exchange for imports approved by Ministry of Finance.	Finance Ministry to authorise grant of foreign exchange to licensed importers.

A. <u>Summary of Objectives</u>

Regulates exchange of hard foreign currencies.

B. <u>Current Constraints</u>

Regulation and control of foreign exchange plays a vital role in imports and exports of all kinds of goods and commodities. Distribution of foreign exchange to various importers and exporters is entirely, by law and in practice, based on HMG/NRB discretion. No clear pattern or stable policy has been evident.

7.	Loan and Guarantee Act	1968	1973 1976 1981	HMG empowered to seek loans from any foreign or international agency for itself or for any incorporated company or firm. HMG authorised to guarantee loans for any organisation and charge for doing so. In case any organisation can not repay its loan, HMG to take responsibility. If the debtor is dissolved, HMG will have priority over the assets, if any, of such organisation to recover the debt. HMG authorised to freeze any assets of a loan-receiving organisation if liquidation appears probable. HMG required to place the agreement concerning the loan received or guarantee given before the Rastriya Panchayat.	HMG National Panchayat (Legislature).

A. Summary of Objectives

This Act enables HMG to seek and receive loans from any bilateral or multilateral foreign agency for itself or for any other organisation in order to meet the demand for capital with a view to financing any development project.

B. Current Constraints

There is nothing in the law that prevents the private sector seeking loans from foreign agencies and HMG acting as a quarantor.

8.	Export-Import Control Act	1955	1963 1972 1974	Power to restrict or prohibit export from or import into Nepal of any good or commodity.	HMG to frame rules, designate licensing authority and prescribe procedures to be followed.
				HMG to regulate and control through promulgation of rules, manner and procedure of licensing, quota suspension or cancellation of license, etc.	Concerned customs officer to prosecute and penalize for contravention of law.
				Provision for maximum imprisonment of 5 years or a fine equal to the amount involved or both.	Concerned Zonal Commissioner to hear first appeal. Second appeal therefrom lies with Regional Court.
9.	Export-Import Control Rules	1977		Designation of export import Controller. Necessary formalities and procedures as to licence, application, fees, etc.	Director-Cum-Controller (Commerce Ministry) to implement the provisions of the law and exercise the powers conferred by the parent act and regulations.

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				Grounds and conditions for grant of license stipulated. Licenses for commercial import and export granted only to duly registered firms and companies. Power to suspend, cancel or refuse licenses.	HMG formulates export/import (trade) policy to be implemented by Ministry of Commerce.

A. <u>Summary of Objectives</u>

The purpose is to empower the government to estrict, prohibit, control and regulate imports into and exports from Nepal of all kinds of goods and commodities through the process and power of licensing.

B. <u>Present Constraints</u>

Absolute discretionary power is exercised by the government. No guidelines exist as to distribution of licenses. Recent introduction of the "Tender or Premium Sale System" has hindered smaller traders in obtaining licenses.

10.	Nepal Rastra Bank Act	1955	1958 1960 1962 1963 1966 1974 1982	Establishment of Nepal Rastra Bank with all necessary power generally available to any central bank. Governor (Ex-officio chairman of the Board), Board of Directors appointed and may be suspended by HMG. NRB regulates and controls foreign exchange. All commercial banks and financial institutions to observe NRB directions. Interests rates on loans and deposits to be fixed by NRB for all Banks/ Financial Institutions. Commercial banks and other banking institutions required to maintain liquidity reserves as may be prescribed by NRB.	HMG to constitute Board, appoint Governor, etc. NRB to frame rules with the approval of HMG.

No company whether private or public allowed to accept deposits without prior approval of NRB.

Notwithstanding anything contained in the Company Act, no company can fix the rate of interest payable to deventure holders or depositors on loan over and above the rate fixed by NRB.

NRB authorised to extend re-loan facility and oblige commercial banks to extend loans to specified sector of economy.

NRB authorised to cause inspection or investigation of any banking institution.

NRB prescribes rates on various banking transactions.

NRB may take any of the following action against any financial institution or banking institution for non-compliance of its directions:

- stop any banks from paying dividends to its shareholders;
- put limits on deposit or loans by commercial banks;
- control and restrict any banking transaction; and/or,
- suspend or cancel banking licenses.

NRB authorised to take direct action against any commercial bank board member or official if found acting against the interest of general depositors.

A. Summary of Objectives

The objective seems to be to establish a powerful central Bank.

B. <u>Current Constraints</u>

NRB seems to be more concerned with the control side of its power if grievances expressed by commercial banks are to be believed. NRB also appears reluctant to permit establishment of finance companies, although the legislature passed the relevant enactment in October, 1985.

11.	Commercial Banks Act	1974	1978 1982 1984 1985	Commercial Bank to operate in money exchange, accept deposits, lend money and perform any other commercial banking transaction other than those reserved for cooperative, agriculture, industrial or similar banks. A commercial bank on recommendation of NRB may be established, registered as per Company Act whose liability is to be limited to shares. Head office of a commercial bank to be fixed with the approval of NRB and by permission of NRB alore it may open or close branch offices. NRB also may direct to it to open or close branches or subbranches at any particular place or area. Foreign commercial banks may open a branch with the consent of NRB but such bank is required to be registered as per Company Act. Before granting such consent NRB must have HMG's concurrence. Board of Directors to consist of maximum of 9 persons to be elected by general assembly of shareholders. Chairman of the B/Ds is to be elected by Board Members by themselves.	The Governor of NRB. HMG. NRB. Ministry of Industries. Supreme Court. Board of Directors.

HMG empowered to nominate all Board Members including chairman in a fully government owned bank. Where HMG has majority, it may nominate 50% of Board Members. However, HMG may delegate its power to NRB authorizing it to nominate 2 directors to former and one to latter banks. In case of a bank other than mentioned above, HMG may nominate 2 directors and this power of nomination may be delegated to NRB. Tenure of Directors is 4 years, and eligible for reelection not to extend beyond three continuous terms.

Board of Directors authorized to perform all functions except those reserved for General Assembly of Shareholders. Board authorised to delegate power to sub-committees or subordinate officials without abdicating its final responsibility.

Share capital and voting rights only ordinary shares to be issued. No share can be sold or transferred to a foreigner without NRB's approval and prior concurrence from HMG. No shareholders irrespective of holdings is entitled to more than 45 votes.

Voting by proxy is limited to 15% of the total shares owned.

Shareholders are entitled to remove or replace any director elected by them through special resolution.

NRB shall be invited to attend Bank's General Assembly meeting as an observer.

Such a meeting cannot be convened unless 15 shareholders representing at least 50% of total shares sold are present.

Bank's paid-up capital not to be less than one million rupees. Paid-up capital not to be less than 50% of issued capital, which cannot be less than 50% of authorised capital.

In order to raise its share capital, a bank is required to obtain approval from NRB. NRB may also direct banks to raise their share capital if it so deems fit.

No Managing Agent allowed to be appointed by commercial banks. No dividend distribution allowed until capital expenditures are recovered.

Opening and operating holding companies except for specified purposes is not allowed.

To operate, banks require permission from NRB which may impose its own terms and, under certain circumstances, cancel permission.

No freezing of money deposited with bank to be done except for funds misappropriated by the depositor.

Auditor General of Nepal to appoint auditor in case of a government owned bank and General Assembly of Shareholders in case of other banks.

Provision for suspension of bank operations by the Supreme Court on the Bank's application for a period not exceeding 6 months.

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Limit on the long-term Bank loans to be fixed by NRB.

HMG, if satisfied with NRB's report, may suspend all or any provision of this Act making it applicable to all or any bank for a maximum period of 6 months. NRB's governor also may exercise this power in emergency situations.

No suit may be filed against any bank employee in connection with misappropriation of bank funds without prior permission of NRB.

NRB to act as arbitrator in disputes arising among one or more banks; NRB's decision to be considered final.

Loans issued by banks valuing less than one million rupees need not be registered and no revenue stamp required.

Banks authorised to recoup its loan by auctioning the property mortgaged.

HMG empowered to remove any difficulty in the implementation of the provisions of the Act by issuing necessary orders.

On matters not dealt with by the Act, ordinary laws in force for the time being to apply.

Banks authorised to frame rules applicable to them, obtaining approval of HMG to do so.

State Commercial Bank Act 1964 and Commercial Bank Act 1963 repealed.

A. Summary of Objectives

In order to consolidate and to provide comprehensive legal provisions governing commercial banks, this Act has been brought into force repealing earlier two enactments.

B. Current Constraints

Commercial Banks in Nepal are concurrently subjected to two sets of laws. It is not sufficient to satisfy all the provisions of the Commercial Banks Act. To be registered as a banking company they must also fulfill all requirements laid down by the Company Act.

C. Possible Improvements

It appears that banking companies should be removed from the control and regulation of the Company Act.

12.	Finance Company Act	1985 Date of enforcement yet to be announced.	Provision for establishing a finance company laid down.	HMG to fix the date of enforcement of the Act.
			Although to be registered as per Company Act, application for registration to go through Nepal Rastra Bank.	NRB to process application, make recommendations for registration. It may impose its own terms.
			NRB may impose its own terms and conditions on a finance company operation. HMG allowed to register and operate a finance company.	NRB authorised to restrict or prohibit a finance company from certain activities.
			HMG may participate as a shareholder in any finance company. Finance companies strictly forbidden to accept deposits from public.	Concerned department may suspend a license on the request of NRB.
			Paid-up capital of a finance company fixed at a minimum of Rs. 25 Lakhs divided into shares of Rs. 100 each.	Regional Court may invoke registration if requested by NRB.

				With the permission of NRB, two or more finance companies may be amalgamated.	Rules to be framed by NRB with the approval of HMG.
				Except for a public company, no one can subscribe to more than 10% of a finance company's shares.	
				Disputes between two or more finance companies to be settled through arbitration of NRB.	

A. Summary of Objectives

The act promulgated to provide the necessary legal provisions for the registration and control of finance companies in Nepal. Power to bring the Act into force has been entrusted to HMG when it deems fit.

B. Current Constraints

No reasons have been announced for the delay in its enforcement. What terms and conditions might be imposed by NRB before making recommendations for registration also are not clear.

C. Possible Improvements

Possible terms which are supposed to be imposed by NRB should be elaborated in the law itself.

13.	Company Act	1964	1968 1971 1972 1973 1984	Incorporation of public private/government companies defined and their conduct controlled through this Act.	Ministry of Commerce to register trading and commercial companies.
				Provision for registration of foreign companies in Nepal.	Ministry of Industries to register and regulate industrial companies.
				Compulsory audit system introduced for all types of companies.	
				Provision for penalties for contravention of the law.	Auditor General of Nepal to appoint auditor for public and government companies.
				Loans raised shall not exceed 50% of the company's paid-up capital.	

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Companies defined:

(i) "Company" means any company incorporated under the Company Act 1964 as a limited company.

(ii) "Private Company" means any company incorporated under this Act with the restriction that it shall not issue invitations to the public to subscribe to its shares and debentures, that any transfer of its shares or debentures by way of security or otherwise shall not be made to persons other than to shareholders without the approval of the Board of Directors, and that the total number of its shareholders shall not exceed fifty.

(iii) "Subsidiary Company" means a company which is controlled by a principal company holding more than 50% shares.

(iv) "Foreign Company" means any company incorporated in a foreign country. Any foreign company which intends to establish a business within Nepal shall have to register itself with the concerned department submitting necessary information and documents.

(v) "Government Company" means, notwithstanding anything provided in other sections of the Company Act, HMG may establish a company whose shares may be sold only to HMG or a corporation owned by HMG. A government company is bound to comply with HMG orders and directions.

(vi) "Public Company" means any company other than a private company. Notwithstanding this general definition, a company otherwise established as a government company (more than fifty-one percent of shares are owned by HMG) shall be called a public company. The provisions regarding the promotors shall not apply in the case of such company.

A. Summary of Objectives

The purpose of the Act is to provide timely and necessary legal provisions for the promotion, incorporation and proper conduct of all types of companies in Nepal.

B. Current Constraints

Currently there is a single enactment for all companies including banks though they are to function under separate banking laws. There is confusion regarding the various types of companies and in actual practice, the existing laws have imposed more obstacles than help or protection. Government companies are by law bound to comply with the orders and directions issued by government. This legal provision has seriously undermined the autonomy of a company in general and more so in the case of a public and government company in particular.

C. Possible Improvements

Banking companies should not be under this Act. Private companies should have a set of laws separate from that for government and public companies.

14.	Private Firms Registration Act	1956	1962 1963 1987	Registration of a firm made compulsory. Procedures laid down for registration, renewal, cancellation etc. Transactions conducted by unregistered firms made illegal. Provision for penalties and power to frame rules delegated to HMG.	HMG to frame rules and designate authority to execute and enforce the law.
15.	Private Firm Registration Rules	1977	1982	Industrial firms to be registered with the Ministry of Industries and trading firms with the Ministry of Commerce. Fees for registration, renewal etc. prescribed.	Ministry of Industries. Ministry of Commerce.

A. Summary of Objectives

Compulsory registration system for all firms engaged in trade and commerce introduced and any transaction made by a firm not duly registered made illegal through this legislation.

B. Current Constraints

As no two firms with the same name can be legally registered, it is imperative that the names of all registered firms be readily known. In the absence of an up to date register, it is difficult for new firms to find whether their name is registerable.

C. Possible Improvements

Annual publication of the names of all firms by official publication of the concerned ministry should be made obligatory.

16.	Industrial Enterprises Act	1981	1984 1985 1987	Compulsory registration of all types of industries with the concerned Ministry. Licensing is compulsory except for cottage industries, small and medium industries that do not require foreign exchange for their main raw materials and any other HMG-specified industries.	HMG. Ministry of Industries. Department of Taxation (Income/Sales). Department of Excise. Department of Customs. Department of Electricity.

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Except defence oriented industries, all industrial ventures made open for private sector participation.	Ministry of Finance. Ministry of Commerce.
Licenses granted on priority basis to HMG specified cottage industries, small scale industries and medium/large scale industries (for companies only).	Revenue Tribunal. Concerned Taxation offices (field).
Definition of various types of industries by class, such as cottage, small, medium and large industries prescribed by law.	
Provision for the constitution of an Industrial Promotion Committee, making it responsible for the recommendations, promotion and encouragement of medium and large scale industries in the private sector.	
Major classifications of industries by their nature and types such as manufacturing, energy-based, special agro-based, mining and mineral processing, tourism, service, assembly are specified.	
Within 8 k.m. of international borders, no industrial ventures are allowed to be established other than cottage industry, industrial districts, tourism, service etc.	
Incentives, facilities and protection in terms of income tax, customs duties, excise duties, sales tax etc. detailed.	

(a) Income tax exemptions:

- Manufacturing cottage industries other than those excepted by HMG: 5 years, 100% exemption from the date of production.

- Small manufacturing industries which need convertible currency for 10% or less of its main raw materials: 5 years exemption.

- Industries specified as producing goods of basic needs or "national priority": 5 years exemption.

- Industries excavating or processing mines and minerals from HMG explored and certified mines: 5 years; mining industries doing exploration and excavation: 8 years.

- Industries formed as public limited companies may claim income tax reduction of an additional 5% over the normal corporate tax.

- Industries offering shares under the Securities Exchange Act 1981 may be entitled to claim a tax rebate of 5% over and above the concession granted above.

- Industries established as other than Public Limited Companies will be subject to a graduated income tax.

- For industries from an "underdeveloped area," rate of tax shall be 5% less; for industries from an "undeveloped area" 30% less.

  (In case of any change in categorisation, existing rates to continue for next 5 years.)

  - Prescribed industries exporting over 25% of annual production: 15% less,

  - Prescribed industries exporting over 50% of annual production: 25% less.

- For expenditure incurred in the expansion of the distribution of goods, advertising and other promotional activities and hospitality expenses etc.: 5% deduction from net income allowed.

- Depreciation on fixed assets: additional 35% over the rate prescribed by income tax law, the amount to be deducted in a lump sum or installments.

- Reinvestment of capital for diversification or expansion of existing capacity by 25% or more: deduction of 25% of the new fixed assets allowed in a lump sum or on an installment basis for a period of 3 years.

- Expenses on product and technology development and increasing efficiency may be deducted from gross income by a prescribed rate.

- Industries employing disabled persons allowed to deduct 25% of the actual wages or salary paid.

- No income tax on dividends of public limited companies.

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(b) Customs duties (normal, premium, surcharge):

- Except for prescribed industrial products, normally no more than 1%.

- For industries from Export Promotion Zones or operating under a "Bonded Warehouse Scheme", no premium, customs duties, excise duties and sales tax on raw materials used to be charged.

- Full refund of excise duties and sales tax paid on products sold to industry and exporters and premium, customs duties, excise duties and sales tax paid on raw materials used in those products.

- Intermediate goods to be used in the production of exportable goods receive refund of premium, sales tax, customs duty paid on raw materials in proportion to exports.

- Industrial enterprises producing new products hitherto not produced in Nepal are exempted from excise duty for 3 years.

- Except for cigarettes, bidis, liquor and some other specified products, all cottage industries products to enjoy excise duty and sales tax exemption.

(c) Special facility:

- Industries contributing to "National Export" by producing high quality goods through the use of modern technology may be accorded special protection and facility.

- Industries exporting more than 50% of their production are required to maintain minimum value added of 10% and other industries 15% ex-factory price basis.

- Restriction on the abuse of facilities, protection and concessions imposed.

- Industrial products sold for foreign currency within Nepal are entitled to refund of excise duties paid by them to the extent of sale in foreign exchange and, premium, customs, duties, excise duties and sales tax paid on raw materials used by such products may also be refunded.

- Products using domestic industrial products where excise duties and sales tax were levied will receive refunds proportionately.

(d) Facility as to convertible foreign exchange:

- F/E may be provided for importation of machinery, spare parts, tools, instruments and other capital goods directly used by industries.

- F/E may be made available to industries on an approved capacity basis for the import of raw materials and auxiliary raw materials, chemicals etc.

- F/E to be provided for the payment of technical consultation charges, technical assistance fees, service charges, management fees, patent royalty, market studies and industrial promotion service charges.

(e) Other incentives:

- No royalty to be charged on power generation by any industry for its own use.

- Industries selling products in the domestic market through international bidding will enjoy all facilities otherwise available to exporting industries.

- For essential machines, equipment and spare parts other than specified by HMG, customs duties may be charged at not more than 5% and no other duties/charges shall be levied.

- Prior approval of HMG is required for modernization, diversification and extension of existing industries.

- Facilities being enjoyed by all industrial enterprises are not to be disturbed by new changes in laws.

- HMG empowered to issue mandatory directives to any industrial enterprises on matters of quality, standard, price, distribution or services, management of closed or under run (below 20%) industrial plants, relationship between management and labor, environment pollution and protection of public interest etc.

- All industrial enterprises required to submit reports to the Ministry of Industry as prescribed.

- HMG empowered to impose fines, suspend or stop giving facilities, run industries by taking it over and may close down any industrial unit if it is found to have ignored its directives or for not submitting reports as asked or abusing the facility accorded or violating the provisions of law.

- System of compulsory arbitration introduced.

- HMG to make rules and may delegate any power available to it to any official or government department.

- Normally, no foreign manpower is allowed to be employed but on non-availability of suitable local manpower, foreigners may be employed with the Labour Department's consent.

A. Summary of Objectives

Primarily, the Act gives effect to and implements the objectives laid down in the Industrial Policy (1981) of HMG. A new Industrial Policy Act will be published in the very near future.

B. Current Constraints

During the five years of its implementation, HMG itself found it irrelevant and discriminatory.

C. Possible Improvements

With the total and far reaching changes made in industrial policy, total revision or amendment of the present Industrial Enterprises Act has become imperative. If HMG is serious about implementing the new policy, it cannot await the Rastriya Panchayat's (National Legislature) annual session held in July. As HMG policy cannot be effected without changing the existing law, ordinances may be promulgated immediately to implement those part of the policy which are not covered by second amendment (1987) of the Act.

17.	Partnership Act	1962	1976 1987	Compulsory registration of a partnership firm of more than one partner to run industrial or commercial enterprise by mutual agreement. Ventures of joint family members not to constitute a partnership firm. No two firms of the same name can be registered. Methods and procedures for registration, renewal, dissolution etc. stipulated. Provision for penalty and appeal, registration fees, etc.	Ministries of Industries and Commerce for registration etc. HMG to frame rules in order to implement the object of the Act.

A. Summary of Objectives

The intention of the law is to make the registration of a partnership compulsory and any dealings done by unregistered firms unlawful.

B. Current Constraints

No rules regulating and describing the manner and procedures for registration etc. have been promulgated after more than 20 years. In the absence of an uptodate publication of the names of registered firms, it is difficult for prospective partners to find a suitable and registrable name.

C. Possible Improvements

The names of private firms, partnerships and companies should be annually published as a matter of general information.

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18.	Foreign Investment and Technology Act	1981	Any investor, foreigner or local or both, requires permission from the Ministry of Industry to establish any industrial enterprise in joint venture.	Ministry of Industry responsible for granting permission and exercising control.
			Prior approval required in order: -to obtain foreign loans; -to increase the ratio of foreign investment; -to enter into a transfer of technology agreement; or, -to diversify the objective, expand the existing capacity or modernise the industrial enterprise or arrange new or additional foreign investment.	Industrial Promotion Committee to be responsible for permission and registration of industrial enterprises.
			Repatriation of profit in foreign currency allowed.	HMG may issue directives/ take action against any industrial enterprise, make rules to enforce the Act.
			HMG also empowered to establish industrial enterprises with foreign or national investors collaboration.	
			Nationalization prohibited except for national interest but not without just compensation.	
			HMG empowered to issue directives to a company: -regarding quality, standard, price and distribution system; and,	

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			-management of industrial enterprises.	
			Provision for arbitration in accordance with UN Rules but Nepalese law to apply.	

A. **Summary of Objectives**

The main objective is to attract foreign investment and technology to accelerate the pace of economic development.

B. **Current Constraints**

By definition, only medium and/or large scale industries come under the purview of this Act. Policy and procedures to obtain permission and to open industries are cumbersome and absolute discritionary power is available to HMG in all matters. The provisions for the use of foreign loans [vide sect 6 (h)] has been interpreted to limit the period of foreign investment itself.

C. **Possible Improvements**

All matters of detail and working procedures pertaining to registration etc. were to be enumerated in the rules but none have been framed. After the recently announced Industrial Policy (1987) Act, most of the legal provisions of this Act are no longer adequate.

19.	Security Exchange Act	1983	Dealing in securities, except by the Security Exchange Centre or by authorised brokers of the Centre is restricted.	Securities Exchange Centre (SEC) only to execute the functions stipulated in the Act.
			Corporate bodies wishing to conduct exchange business must be registered by a Security Exchange Centre.	Ministry of Industries empowered to register/refuse/suspend or cancel such registration at its discretion.
			Public companies or corporate bodies are authorised to issue securities to the general public only through the SEC.	Ministry of Industries to appoint not more than two SEC Directors,

					may issue directives or orders, may on its own or through Nepal Rastra Bank or anybody else conduct investigations/ inspections of SEC.
				Brokers may be appointed by SEC.	District Court to exercise original jurisdiction in all cases filed under this Act.
				HMG securities issued under the Public Debt Act 1959 are excluded from the purview of this Act.	
20.	Securities Listing Regulation	1983		Detailed provisions for listing procedures, condition of ownership and allotment of securities, etc. laid down.	HMG to frame rules governing securities listing etc. SEC to conduct listing operations.

A. Summaries of Objectives

Enacted to systematise and regularise securities dealings, to protect the interests of investors and to mobilize private capital for industrial enterprises.

B. Current Constraints

The SEC is asked to perform a host of functions - distributor, regulator, revenue agent, investment advisor, broker etc. To date no brokers have been licensed. The control to be exercised by Nepal Rastra Bank is not clearly defined.

C. Possible Improvements

The SEC's multiple functions may in time need to be shared among other public/private institutions.

21.	Nepal Industrial Development Act	1959	1963 1965 1985	NIDC to provide long term industrial loans to entrepreneurs/individuals/ firms/private/public	HMG to frame rules for the enforcement of the Act, to

companies, to provide promotional services on matters of a project's technical or economic viability to encourage purchase of NIDC shares or debentures, to enter into banking transactions with national or foreign banks.	appoint a Board of Directors including the Chief Executive, to approve regulations framed by the board.
Out of six members of the Board of Directors, two must be nominated by the general annual meeting from among private businessmen/industrialists.	General Meeting to nominate two private members to Board.
Provision for penalty for contravention of the Act, which may include imprisonment and/or fine.	Board to frame by-laws for NIDC internal administration as well as for the implementing of the Act.
	HMG may institute an inquiry into the workings of NIDC if deemed necessary.
	NIDC to work as per the directives and policies issued by HMG.

A. Summary of Objectives

The Act is intended to establish an industrial bank, thus encouraging private sector industrialists to establish and operate ventures which contribute to the rapid industrialization of the country.

B. Current Constraints

Effective implementation of the NIDC Act depends upon the creation and maintenance of a conducive industrial climate by the government through its industrial policies and on unbiased implementation of other rules and regulations guaranteeing incentives. However, experience shows that these policies and laws are not always stable and, many times, they are paradoxically contradictory.

C. <u>Possible Improvements</u>

With the change in industrial policy, all laws relating to industrial activities including industrial lending need a thorough review and, probably, amendment.

22.	Income Tax Act	1974 1977 1979 1980 1984 1985 1986	Provision for appointment of tax officers and delegation power laid down, classification of sources of income (agriculture, industry, business, profession or vocations), remunerations, building, land rent etc. specified.	HMG to frame rules, appoint tax officials.
			Any person intending to carry on any occupation after having registered as a private firm, partnership firm, company or in any form, must register with the concerned tax office.	Director General, Chief Tax Officer or Tax Officer. Tax Assessment Committee.
			Method of computing net income laid down in detail.	Revenue Tribunal.
			Rents payable, expenses, interest on loans, land tax, custom duties, registration fees, transport or traveling expenses, administrative expenses, discount or commission, etc. allowable deductions from gross income.	
			Method of computing net income from insurance business enumerated.	
			Assessment of small taxpayers prescribed by separate rates.	
			Computation of net-income by agreement in certain situations authorised.	
			Tax due from a firm or partnership, although assessed in the name of such firm, is collected from the proprietors or partners.	

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Tax officer is empowered to require any person, firm, company, bank, financial or any other institution, governmental or non-governmental office to furnish any information regarding sources of income or business of a particular taxpayer.

In case of non-Nepalese or non-resident taxpayers, tax may be collected in advance.

HMG may by notification require certain classes of taxpayers to pay tax in advance as per statement submitted before assessment.

Any office or person paying remuneration, rent, commission, bonus, share of profits, interest, etc. may be required to deduct tax therefrom at source.

Provision for imposing fees (3-7%) and a fine (5%) for delay or default in tax payments.

HMG empowered to imprison any taxpayer up to 6 months for default in payment of tax.

No claim for refund to be entertained after 2 years.

HMG empowered to constitute an Assessment Committee.

Following deductions are not allowed:

-any capital expenditure or capital loss incurred.

-any expenditure by way of remuneration, interest, rent or bonus by other than a public limited company to partners or members.

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			Industrial enterprises to get income tax exemptions in full or part as provided in relevant industrial enterprises acts.
			Power to inspect, search and seize any records vested in HMG.
			HMG empowered to make agreement with any foreign government to avoid double taxation.
			Accounts and relevant documents need to be preserved for 6 years from the date of assessment of tax, and HMG may compel any taxpayer to have his accounts audited.
			Auditors certifying false accounts may be prosecuted and penalised.
			HMG empowered to make a reassessment or supplementary assessment within 5 years of earlier assessment.
			Right to appeal assessment to the Revenue Tribunal reserved.
			HMG empowered to prohibit sale or transfer of movable or immovable property until the concerned taxpayer produces receipt of tax payment, certificate of tax exemption or tax clearance.
23.	Income Tax Rules	1982	Taxation offices established and their jurisdiction delineated.
			Procedures for obtaining clearance certificate and submission of statement.
			Special provisions for assessment of income tax on small traders enumerated.

Forms and details regarding assessment etc. laid down.

A. Summary of Objectives

Enacted to consolidate and lay down comprehensive legal provisions regarding determination, assessment and collection of taxes, and repealing the prior Income Tax Act.

B. Current Constraints

Tax authorities given enormous powers in matters of tax assessment. Procedures are lengthy and complicated. Exemptions granted under relevant industrial enterprise laws are not made available. Recommendations made by the Ministry of Industries may not be accepted by the Department of Income Tax. Mistakes or wrong interpretations even after correction by a higher authority are not rectified. Authoritative interpretations given by courts are not followed.

C. Possible Improvements

Tax law, manuals and official procedures need wholesale review and simplification. The provision making directors of a closed or liquidated company personally responsible for payment of tax due is contrary to the concept of corporate personality and norms of limited liability.

24.	Sales Tax Act	1966	1974 1983 1984	Provisions laid down for fixation and collection of sales taxes. Sellers of all products require to register and obtain certificates from tax office to collect tax. Unregistered sellers of goods required to furnish statements of stocks of goods. Collected taxes to be deposited within the Nepal Rastra Bank within 45 days of the end of each month. Tax officer authorised to make "best judgement" assessment. Tax officer to exercise all powers ordinarily available to a regular court of law in matters of prosecution, proceedings etc.	HMG. Tax Office. Department of Taxation.

				HMG empowered to exempt certain categories of goods.	
25.	Sales Tax Rules	1967		Procedures laid down for furnishing of statements, sales tax collection, certificates, etc.	Tax officer. Tax Department. Ministry of Foreign Affairs.
				Determination and deposit of sales tax procedures stipulated.	Ministry of Finance.
				Persons enjoying diplomatic privileges required to obtain certificates to that effect.	

A. Summary of Objectives

The Act and rules are meant to lay down necessary provisions and procedures for collection, deposit and exemption of sales tax.

B. Current Constraints

The exemption and concessions which the relevant industrial enterprises acts have laid down in matters of sales tax are not explicitly reflected in this act. This leads to contradiction and confusion. Recommendations made by the Ministry of Industries or Cottage and Small Scale Industries are not accepted by the Department of Taxation. Generally, taxes on industrial raw materials are levied at the customs point in advance. Due to different interpretations by the Ministry of Industries and Department of Taxation, entrepreneurs are compelled to go to court for an authoritative resolution. Even after favourable court decisions, tax officers often continue to repeat their previous actions.

C. Possible Improvements

All laws providing concessions, incentives or any other exemptions should be drafted in a clear and unambiguous manner so that there is little room for misinterpretation or divergent interpretations. Recommendations in matters of exemptions made by the Ministry of Industries or Cottage and Small Industries should be binding on the Department of Taxation.

26.	Customs Act	1962	1963 1964 1965 1969 1971 1974 1985 1986	Enacted to make uniform and consolidated custom regulations. Provisions for fixing and collecting custom duties on exports/imports.	HMG. Ministry of Finance Various customs officers.

			Customs authorities empowered to value exports/imports at their discretion for their purpose.	Revenue Tribunal. Regional Court.
			HMG empowered to purchase any imports if found underinvoiced.	Supreme Court.
			HMG authorised to grant exemption or reduce the rate of customs duties on any item.	
			Custom officer empowered to search and seize any goods on reasonable suspicion.	
			Power to take possession and confiscate contraband goods.	
			Provision for penalty and prosecution.	
			Provision for appeal from the original order.	
			HMG empowered to frame rules.	
27.	Customs Rules	1970	Provision for Customs Agent.	
			Custom clearance procedures prescribed.	
			Rules and procedures regarding customs godown etc.	

A. Summary of Objectives

The object of Customs Act and Rules is to lay down specific provision to be followed by custom officials and concerned individuals when importing into and exporting from Nepal.

B. Current Constraints

One of the main complaints lodged against existing customs procedures has been that they are very complicated, time consuming and costly. In the absence of clear, simple and short procedures, customs officials enjoy arbitrary powers which permit harassment of importers and exporters. Those powers can also be used to the personal advantage of officials and against the interest of revenue collection.

C. <u>Possible Improvements</u>

The provisions of law should be drafted in such a manner that they are free from possible divergent and arbitrary interpretation. The provisions regarding valuation of goods should be based on known and reasonable criteria.

28.	Excise Act	1958	1960 1964 1974	HMG empowered to fix rate of excise on any product through gazette notification and to prescribe the manner of its levying. No one is allowed to operate any industry without a license from the concerned excise office. Procedures for obtaining license provided. Power of arrest and take-over of any industrial products given to excise officer. Power of HMG to frame rules. Power of HMG to exempt any industrial product maximum of 3 years in the interest of the country's industrial development. Provision for prosecution, penalty and appeal.	HMG to fix products as excisable, frame rules/ grant exemptions. Excise Dept. Area excise officer to enforce provisions. Revenue Tribunal to hear appeal of excise officer's order. Ministry of Industries.
29.	Excise Rules	1962		Elaborate provisions for designation, powers and functions of excise officers. Procedures for obtaining and granting license, periods of validity and renewal, etc. stipulated. License fees prescribed for certain products such as matches, soap, cigarettes, sugar, etc. Rights and duties of factory inspector and industry owner laid down.	Excise Officer. Inspector.

A. Summary of Objectives

The purpose is to provide necessary legal provisions with regard to imposition, collection and general administration of excise duties payable by industries.

B. Current Constraints

There is no coordination between Department of Excise and Ministry of Industries. As a consequence, exemptions granted under the Industrial Enterprises Act and declared government policy are denied to concerned industries. Very often companies are compelled to move to the highest courts to claim their rights.

C. Possible Improvements

If any excise exemption is available under the industrial policy and Industrial Enterprises Act, the certified recommendation of the Ministry of Industries should be accepted as final and binding on the Department of Excise.

30.	Provisional Tax Collection Act	1954	1980	HMG empowered to revise or amend any laws relating to customs duties, excise duties or like at any time on a provisional basis. Provisional taxes to be levied by executive order and to remain operative until amended by legislature sitting immediately after issue of such an order or not revoked by HMG.	HMG. Rastriya Panchayat. Customs/Tax/ Excise Officers.

A. Summary of Objectives

The Act enables HMG to impose any charges in the form of taxes.

B. Current Constraints

Tax rates are generally revised through annual fiscal laws, and businesses plan their industrial or trading activities on that basis. Sudden changes in tax rates or duties may have adverse effects.

C. Possible Improvements

In view of Article 57 of the constitution (which exists for the same purpose) there is no need or rationale for keeping this Act on the statute books.

31.	Contract Tax Act	1966	1974 1986	Collection procedures in matters of contract tax laid down.	HMG. Tax Officers.

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			Act also applies to foreigners who are working as contractors in Nepal.	Revenue Tribunals.
			Statements regarding contractual agreements must be submitted within 7 days of agreement to the concerned tax office.	Higher Courts.
			Stipulations relating to assessment of taxes and penalties for giving false or incomplete statements elaborated.	
			Tax officer to exercise all power available to regular courts.	
			Contract tax to be collected at source.	
			HMG authorised to exempt contract tax in certain cases and frame rules.	
32.	Contract Tax Rules	1966	Schedules and other procedures regarding collection of contract tax prescribed.	

A. Summary of Objectives

In order to facilitate the collection of taxes from contractors, the Act provides for collection at source.

B. Current Constraints

The law does not reflect concern about the interests of contractors other than revenue. In case of termination or breach of contract taxes collected in advance may create difficulty in that it is not that easy to get refunds once taxes are deposited in government accounts.

C. Possible Improvements

Reconsideration of the need for a special Act relating to contract tax.

33.	Acquisition of Lands Act	1977	HMG is empowered to acquire or nationalise any landed property if deemed necessary to conduct any public welfare work for itself or for any organisation.	

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Under the provisions of this Act, HMG is authorised to acquire and the concerned company/corporation or Development Board entitled to ask for any land to be acquired.

Mode of acquisition, method of calculating compensation and procedures for receiving compensation also laid down.

Power of State to acquire land or landed property can be utilized by any private or public company if this leads to general public benefit.

Lands acquired for one purpose may be utilized for other purposes or returned to its original owner if not found essential.

Provision for execution of scheme of acquisition, prosecution and penalty for obstruction or non-observance of the orders prescribed.

A. Summary of Objectives

The main objective of the enactment is to provide necessary legal provisions for acquiring lands to carry out development projects.

B. Current Constraints

Law is discriminatory in that there are two sets of rules for calculating compensation, i.e., one for the land acquired for HMG or HMG owned corporate bodies and the other for non-governmental bodies or private companies. Rates of compensation also are generally not based on market value.

C. Possible Improvements

The Requisition of Immovable Property Act (see hereafter) and this Act should be amalgamated and basic principles be laid down in one comprehensive act. Powers and procedures should be defined and procedures streamlined. HMG (cabinet) should have the power to authorise acquisition to ensure fundamental property rights of an individual. Land or property not used for the purpose it was acquired, if possible, should be returned to the original owner. The procedures and manner of distribution of compensation and mechanism for filing objections against acquisition could be improved.

34.	Requisition of Immovable Property Act	1956	1961 1963	HMG empowered to requisition any immovable property if deemed in the public interest immediately or subsequently.	HMG.
					HMG designated officer.
				The property owner may be given time to file an objection.	A judge as an arbitrator.
				Order not open to challenge in any court of law.	
				Owner of the property to be compensated ordinarily at market value.	
				On questions of compensation, if not settled through negotiation and agreement, a retired or sitting judge may settle the issue as an arbitrator.	
				Property requisitioned may be released.	
				HMG may delegate its power to any of its official in a manner and with terms of delegation as specified in the official gazette notice	
				HMG authorised to frame rules in order to carry out the purpose and objective of the parent Act.	
				Provision for penalty for obstructing the requisition process.	
				Any owner who generally resides outside Nepal and/or has invested his major property outside the country shall not be entitled to compensation.	

A. <u>Summary of Objectives</u>

In order to make requisition of any immovable property HMG has been given the necessary legal power, and the principles of compensation and procedures for requisition also have been laid down.

B. Current Constraints

Any property requisitioned under the authority of this Act seems to belong to the HMG only for a temporary period. The Acquisition of Land Act 1977 (by definition "house" is also included) which is more recent and comprehensive, serves the same purpose.

C. Possible Improvements

Requisition of Immovable Property Act 1956 and Acquisition of Lands Act 1977 should be combined into one comprehensive and consolidated law. Proper reconciliation between this Act and the Industrial Enterprises Act, especially in matters of nationalization of industrial properties, should be made.

35.	Land Revenue Act	1976	1983	Land Revenue Collection Offices for each of 75 districts established to collect land revenue on an annual basis. Each land Revenue collection office to maintain and register all kinds of lands within its jurisdiction. Land revenue offices empowered to freeze the transfer of ownership or sale by auction of such lands to recover dues authorised. Procedures regarding waiver of revenue in certain cases laid down. HMG empowered to make rules. Without obtaining approval from committee, no government land or unclaimed land to be utilized. Provision for punishment and appeal.	HMG. Ministry of Finance. Department of Land Revenue. Land Revenue. Zonal Court.
36.	Land Revenue Rules	1980		Procedures for preparation of land records and sale of government land laid down. Procedures for sale of lands by auction stipulated.	

Power, function and duties regarding collection of land revenue enumerated.

Provision for claiming new lands.

New and unclaimed lands to be distributed on priority basis by HMG.

Lands distributed under rehabilitation programmes also to be registered by each Land Revenue Collection Office.

A. <u>Summary of Objectives</u>

The Land Revenue Act and rules framed by HMG thereunder provide necessary legal arrangements and procedures regarding collection of land revenue, powers and functions of land revenue offices.

B. <u>Current Constraints</u>

One of the main functions of land revenue collection offices is to maintain an up-to-date registry system. Ownership of landed property is decided on the basis of such records. But, due to defective administration, each transfer of ownership creates a new dispute.

C. <u>Possible Improvements</u>

A system of up-to-date record keeping should be introduced to replace present dispute-generating methods.

37.	Nepal Factory and Factory Workers Act	1959	1960 1961 1962 1974 1978	Any factory or establishment having ten or more workers falls under the purview of this Act. Factories are to pay minimum wages and ensure employee safety and welfare as stipulated in the Act. Employment of alien labour is generally forbidden. Appointment of Factory Inspectors and Labour Welfare Officers by HMG. Representation of labour unions in the management of a factory provided.	HMG to frame regulations. Ministry of Labour Welfare and Dept. of Labour Welfare responsible for implementing the law. HMG to fix and revise minimum wages; it may withdraw or extend the scope of the Act to any industrial establishment.

38.	Nepal Factory and Factory Workers Rules	1963	1978	Details specified regarding the principles laid down by the parent Act.	

A. Summary of Objectives

In order to maintain peace and tranquility and ensure the economic welfare by making suitable arrangements concerning the proper management of factories, the safety and comfort of factory workers and settlement of disputes between workers, owners and management, this law was introduced and is being implemented.

B. Current Constraints

Going strictly by the original intent, the Act was basically meant for industrial factories and workers engaged therein. But, under the power vested in HMG by Sect. 60 B, the scope of the Act has been extended to cover any entity such as a restaurant, hotel, transport service etc. which has lead to difficulties in the application of law.

C. Possible Improvements

It would be preferable to have separate labour welfare laws and regulations for different sectors.

39.	Bonus Act	1973	1977	Profit making organisations (private or public) required to distribute a bonus to employees amounting to 10% of profits. Any factory or organisation having 10 or more employees and more than Rs. 2 lakhs in fixed capital must comply. The manner, grounds and procedures for distribution prescribed. Under certain conditions, advance distribution of bonus is to be made. Duties and personal responsibility of a manager of an organisation on failing to observe these provisions established. Settlement of disputes regarding the bonus issue by or through the Labour Department; failing to do	HMG to specify the date of enforcement of Act, frame rules, issue directives and constitute a Tribunal. Labour Dept. to supervise the law. HMG constituted tribunal to settle disputes referred to it.

			so, to be referred to a HMG constituted tribunal. Rules to be framed to execute the purposes of the Act. Provision for complain and penalty.	
40.	Bonus Rules	1982	Balance sheet and income & expenditure accounts of a concern to be submitted within 6 months after the fiscal year ends. Provision and procedure for making complaints against false or wrong accounts. HMG organisations (other than non-profit making bodies rendering promotional services in the field of administration, industry and agriculture) obliged to set aside funds for an 8% of net profit bonus. Government trading or management enterprises enjoying monopoly positions are obliged to set aside bonus money, which may be specified by HMG from time to time. Constitution of a welfare committee and use/operation of welfare fund prescribed.	Welfare Committee to operate welfare fund. HMG to revise or amend the rules. HMG to fix minimum rate and amount of bonus applicable to certain govt. owned organisations.

A. Summary of Objectives

Establishes a required bonus distribution by private and public sector organisations.

B. Current Constraints

HMG has not yet enforced the law throughout the country. There may be more eligible enterprises in other geographical areas to which the law has not yet been applied.

C. Possible Improvements

Mandating different rates of bonus for private and public enterprises is questionable.

41.	Lands Act	1964	1965 1967 1980	Ceiling on land to be controlled by owners and tenants.	HMG to frame rules, appoint land reform officers, and issue necessary orders and directives.
				Lands in excess of prescribed ceilings taken over by the state.	HMG to exempt industries from land ceiling laws.
				For the lands taken over by the state in excess of ceiling, compensation to be paid by HMG to the owner.	Land Reform Offices. Regular Courts
				Lands confiscated may be distributed to landless people at fixed prices paid in installments.	
				Tenancy right guaranteed through necessary legal safeguards.	
				System of fixed rents introduced to encourage and increase production.	
				Lands if used to develop prescribed industrial or agricultural industries may be exempted from the ceiling.	

A. <u>Summary of Objectives</u>

The basic objective of the Act was to introduce and protect tenancy rights, abolish landlordship (Zamindari system) system, impose ceilings on land holdings, fix rates of rent and ultimately encourage people to shift their otherwise idle capital gradually to other industrial productive ventures.

B. <u>Current Constraints</u>

Provision for exempting from the ceiling lands if used for industrial purposes has not been implemented and administered properly. There are no general or specific guidelines as to precisely what industries are to be granted this exemption. Neither has agriculture production increased nor the capital from the agriculture sector been found to have been transferred in other productive industrial sector. Indirectly, it has contibuted to discouraging agro-based industries.

Possible Improvements

Exemption from the ceiling should be in line with the declared industrial policy of HMG. The Lands Act should be amended so that all industrial enterprises qualify to acquire and own lands for their use once they are registered as per the Industrial Enterprises Act.

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Appendix D

OTHER LAWS REVIEWED GOVERNING PRIVATE ENTERPRISES IN NEPAL

	Title	Year Promulgated
1.	Development Board Act	1956
2.	National Transport Systems Act	1969
3.	Communications Corporation Act	1972
4.	Gorkhapatra Corporation Act	1963
5.	National News Agency Act	1962
6.	Nepal Agency Act	1958
7.	Nepal Agency Rules	1962
8.	Ban on Investment in Foreign Countries Act	1964
9.	Liquor Act	1974
10.	Black Marketing and some other Anti-Social Activities (punishment) Act	1975
11.	Tax Arrears & Clearance Commission Act	1976
12.	Industrial Trainees Act	1981
13.	Tourism Act	1978
14.	Nepal Electricity Authority Act	1984
15.	Contract Act	1966
16.	Revenue Tribunals Act	1974
17.	Passport Act	1967
18.	Passport Rules	1971
19.	National Insurance Corporation Act	1968
20.	Insurance Act	1968
21.	Libel and Defamation Act	1959
22.	Civil Rights Act	1955
23.	Cooperative Societies Act	1984
24.	Revenue Stamp Act	1963
25.	Road Taxes Act	1961
26.	Entertainment Tax Act	1961
27.	Entertainment Tax Rules	1962
28.	House Tax Act	1963
29.	House Tax Rules	1963
30.	House and Land Rent Tax Act	1966
31.	House and Land Rent Tax Rules	1967
32.	Vehicle Tax Act	1974
33.	Vehicle Tax Rules	1977
34.	Foreigners Act	1958
35.	Foreigners Regulation	1974
36.	Societies Registration Act	1977
37.	Societies Registration Regulation	1978
38.	Soil and Watershed Conservation Act	1982
39.	Patent, Design and Trademark Act	1965
40.	Audit Act	1961
41.	Town Development Plans (Execution)	1973
42.	Government Contract Act	1962
43.	Arbitration Act	1981
44.	Nationalization of Private Forests Act	1957
45.	Forests Act	1961
46.	Corporations Act	1964
47.	Nepal Petroleum Act	1984
48.	Donation Act	1975
49.	General Principles Pertaining to Appointment, Promotion and Departmental Actions in Corporate Bodies	1986
50.	Export-Import Control Notification	1984

Appendix E

SECURITIES EXCHANGE CENTRE LTD.
NEW ISSUES

Issuing Company	Year Offered	Type Security	Par Value	Amount Offered (Rs000)	Share Limit	Percent Subscribed	No. of Subs-cribers
Balaju Yantra Shala Electro	1977/78	Share	Rs. 100	Rs. 94.5	N.A.	118.0%	N.A.
Hetauda Leather	1978/79	Share	100	1991.0	None	40.4	38
Agriculture Dev. Bank	1978/79	Deb.	1000	40000.0	-	100.0	N.A.
Nepal Metal Co.	1979/80	Share	10	4200.0	None	2.7	N.A.
NIDC	1981/82	Deb.	10000	40000.0	-	100.0	N.A.
NIDC	1982/83	Deb.	10000	40000.0	-	100.0	N.A.
NIC	1983/84	Share	100	2400.0	50	40.6	505
Nepal Battery	1983/84	Share	100	4000.0	N.A.	175.4	33
NIDC	1983/84	Deb.	10000	40000.0	-	100.0	N.A.
Agriculture Dev. Bank	1983/84	Deb.	1000	40000.0	-	50.0	N.A.
Nepal Arab Bank	1984/85	Share	100	15000.0	1500	263.0	5,072
Nepal Trading Co.	1984/85	Share	100	7314.7	None	4.3	66
Nepal Lube Oil	1984/85	Share	100	1792.0	500	300.[illegible]	613
NIDC	1984/85	Share	100	10000.0	None	23.0	375
Himal Cement	1985/86	Share	100	10923.3	None	17.5	367
Nepal Indo Suez Bank	1985/86	Share	100	12000.0	500	374.8	2,783
Nepal Grindlays Bank	1986/87	Share	100	7500.0	100	540.5	5,035
Bottlers Nepal	1986/87	Deb.	1000	50000.0	-	102.5	230

*Fiscal year ending July 15.

Appendix F

SECURITIES EXCHANGE CENTRE LTD.
MARKET OPERATIONS

Issuer	Fiscal Year 1987 No. of Trans-actions	Ave. No. Shares	(Rs.000) Total Value	1st Quarter 1988 No. of Trans-actions	Ave. No. Shares	(Rs.000) Total Value
Nepal Bank	95	9.2	274	15	4.5	33
Nepal Insurance and Transport	13	54.2	215	2	5.0	6
Bishal Bazar	120	39.8	2298	50	88.8	2,564
Salt Trading	77	25.0	777	-	-	-
Nabil Bank	47	24.3	100	2	10.0	2
NIC	18	14.6	118	2	5.0	6
Nepal Plywood	2	10.5	3	3	133.3	21
NIDC	20	5.8	16	4	6.0	6
Nepal Battery	3	533.3	298	3	52.5	21
Himal Cement	9	36.0	67	-	-	-
Bottlers Nepal	1[illegible]	73.0	3,942	7	17.6	369
Nepal Lube [illegible]	6	29.2	23	2	20.0	5
Nepal Indo [illegible]	-	-	-	1	20.0	1
	428		8,126	92		3,068