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Leveraging Federalism

Economic Growth and Doing Business for Prosperity

Jai Venaik
Sambriddhi Acharya, Sujan Regmi

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ABBREVIATIONS AND ACRONYMS

AP	Andhra Pradesh
BoP	Balance of Payment
CA	Constituent Assembly
CDP	Committee for Development Policy
CPN-MC	Communist Party of Nepal - Maoist Centre
CPN-UML	Communist Party of Nepal – Unified Marxist Leninist
CSRDSP	Committee on State Restructuring and Division of State Power
EVI	Economic Vulnerability Index
HAI	Human Asset Index
FPTP	First-Past-the-Post
GDP	Gross Domestic Product
GNI	Gross National Income
GoN	Government of Nepal
INR	Indian Rupees
IT	Information Technology
Km	Kilo meter
LDC	Least Developed Country
LLDC	Land Locked Least Developing Countries
MICE	Meetings, Incentives, Conferences and Exhibitions
MAUD	Municipal Administration and Urban Development
MoU	Memorandum of Understanding
MW	Mega Watt

NC	Nepali Congress
NPC	National Planning Commission
NPR	Nepalese Rupees
NRB	Nepal Rastra Bank
NRI	Non-Resident Indians
OCR	Office of Company Registrar
PEMANDU	Performance Management and Delivery Unit
PLA	People's Liberation Army (of Nepal)
SAARC	South Asian Association for Regional Cooperation
TS-iPASS	Telangana State Industrial Project Approval and Self-Certification System
UN	United Nations
UNDP	United Nations Development Programme
US	United States
VDC	Village Development Committee

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EXECUTIVE SUMMARY

It has been a little over two years that Nepal has adopted a new federal republic constitution. This major transition in Nepal's political history did not come by easily. Over a decade of armed conflict and subsequent protracted political process that also lasted almost 10 years, finally gave the country a new constitution. There were doubts whether this constitution would be implemented at all, given the opposition that erupted following the announcement of the passage of the constitution by a majority vote. However, the successful elections of all three levels (Federal, State and Local) of government in lengthy five phases have now raised hopes that this country will finally achieve the long-awaited political stability. We are now at the beginning of implementation phase of the federalism in Nepal.

The report is designed to aid law-makers, intellectuals, students, universities and general population in making informed analysis of potential roadblocks in the implementation of federal system of governance. Nepal cannot afford to relapse into another phase of armed conflict or wide-spread social discontent. Therefore, it is imperative that we become proactive in identifying potential problems and working out solutions before the problems become severe. It is in this backdrop that this report specifically focuses on business development in Nepal in relation to a few economic sectors and regulatory mechanism.

Nepal ranks 105 out of 190 countries on World Bank's Ease of Doing Business index 2018. While it ranks generally above average on registration of property and protecting minority investors, it performs abysmally on issues of dealing with construction permits (157), enforcing contracts (153) and paying taxes (143).

Nepal is a low-income country by development classification. Although Nepal has met two of the three indicators used to graduate a country from a Least Developed Country (LDC) to a developing country status in two consecutive evaluations, the per capita income remains still low. And, there are no signs that the third criteria can be met in the next three years.

Federalism is specifically aimed at transforming the unitary structure of governance so that more powers are given to the sub-national governments. As per the new constitution, the nation now has seven states and seven hundred and fifty-three local governments and one federal government. The new constitution, along with the three orders of government, are constitutionally entrenched and autonomous in character. Various constitutional, historical, economic, social, cultural, geographical and political factors greatly influence this federal character. From its inception in modern history (1950) to present day (2018), Nepal has witnessed severe political instability, especially in the last two decades. After a long spell of autocratic regimes spanning over a century in the modern history of Nepal, stable multi-party democracy was introduced in 1991. It was not the first time that democracy was introduced in Nepal. The 1959 attempt of democratic governance was aborted in just about two years by royal takeover.

The political system has also seen variations over the years— absolute monarchy (1948) to a democratic system (1950-1959), a return to absolute monarchy (1962-1989) followed by a constitutional monarchy with multi-party democracy (1991). This was interrupted by an armed conflict (1996) followed by an absolute monarchy (2005) with the suspension of Parliament. The crisis came to an end with the end of the 240 years of monarchy and the country was turned republican and federalised (2007, 2015). The vast variation in the constitutional provisions that have existed in the past bears significance to the resultant provisions that form a part of the new constitution and hence, are studied to inform analysis. The key takeaway from the discussion pertains to the degree of centralization in the current constitution. Though heavily decentralized, the current constitution still retains a central character in its framework.

A triumph of the current architecture is manifested in the form of justiciable fundamental rights for citizens, and clear directions for the future government/s to form policies on through the directive principles and obligations of the state. A prime example of this is the freedom of every citizen to earn his/her living and also make use of his/her property to live a dignified life. The state is also directed to ensure prosperity for the country by aiding citizens in every aspect possible to be able to achieve prosperity at an individual level; for the country would only prosper if the individuals living in it prosper.

A cross examination of the various key economic indicators at sub-national (state and local) levels helps us dissect key areas where individual units should concentrate to effectively harness the potential that human and natural resources may offer. The literature review informs us of the urgent need to develop policies in a framework that would help the common man ease the process of conducting business in Nepal. Specifically, the literature points to the principle of subsidiarity i.e. a task should be awarded to the lowest possible jurisdiction that can handle the task without causing spill-over effects and externalities. It additionally highlights the advantage of a healthy competitive spirit that the federal form brings to advance growth. Furthermore, a strict fiscal discipline and a common market are also required to ensure a sustainable growth environment for the economy to advance.

This paper uses the performances of 13 federal countries which assign different competencies to different jurisdictions to paint a general picture. This matrix also helps draw important conclusions on the possible steps to that can be taken on the basis of international best practices, and also hint at the possible road blocks that could occur during the implementation phase. The components of the doing business index prepared by the World Bank are further analysed given the new architecture and division of powers in Nepal's new structure. While it can be inferred that construction permits and registration of property are responsibilities of the local government, trading across borders and resolving insolvencies would largely be influenced by the federal government. Most other indicators such as: labour market regulations, access to credit (among others) would be joint competencies of

the federal and state governments with the exception of paying taxes which would be shared by all three levels depending on the type of tax and the jurisdiction they fall under.

The general observations concerning Nepal's federal structure are: it takes form of a symmetrical division¹, a heterogeneous society (w.r.t. ethnic divisions, communities) with homogenous components (school system, prevalence of spoken Nepali in some form), a parliamentary system (federal and state) and a quasi-presidential governance (local) amongst a heavy concurrency² dependent model. These concepts along with functional assignment of subjects (or competencies) are analysed when comparing with the sample countries. This is followed by the sectoral analysis of five broad sectors, and within each, the following potential road blocks were inferred:

1. Banking and Financial Institutions

- A. There is no clear differentiation between the federal and state governments' scope of powers on the operational policy of banks and financial institutions.
- B. The scope of Central Bank's role and the differences in states' policies on operations of banks and financial institutions.
- C. The lack of a strong legislation governing co-operative sector and non-NRB-controlled financial institutions (both formal and informal in nature).

2. Labour Markets

- A. The possibility of an unjust federal pavilion controlling trade unions and an inhospitable employee-employer relation due to political inference.
- B. The need for cross-border labour legislation.
- C. The need for localized skill development policies required to improve the human resource capacity of the country.

¹ a symmetrical division does not have separate laws and laws applicable to the sub-national units in a federal system of governance.

² When powers are shared between two or more levels of government they are called concurrent powers

3. Business Corporations

- A. Public sector enterprises enjoy preferential treatment which in turn promote anti-competitive activities. Thus, an equal treatment of public and private enterprises through same laws with no preferential treatment via a singular system of laws.
- B. The need to amend the earlier business laws and reflect the responsibilities of all orders of the government thereby reduce federal dominance.
- C. The need to counter anti-competitive activities fostered by associations and syndicates which act as cartels and inhibit the entry of new players and innovations in service delivery.

4. Agriculture

- A. The lack of clear roles regarding the exact nature and scope of responsibilities amongst the three orders of government may lead to inter jurisdictional conflict.
- B. The case of value chain industry activity and incoherence in laws regarding policies and taxation lead to roadblocks in the sector.
- C. The lack of a financing model that is essential to spruce up the sector.

5. Tourism

- A. The de-concentration³ of federal agencies or creation of agencies/bodies at sub-national levels to help facilitate economic activity in the sector.
- B. Issues of inter-state tourism, specially in the case of trekking and mountaineering, which have spill over effects. An umbrella Act is currently non-existent in Nepal.

³ Deconcentration is a term used to describe the process whereby a central organization transfers some of its responsibilities, organs or departments to lower-level units within its jurisdiction.

1. Drawing from lessons from other federations and expertise of key stakeholders in these areas, following issues have been identified as ones that need to be deliberated over in order to create a more conducive environment for smooth implementation the Constitution: Restructuring of legislative lists to provide clarity in the roles and responsibilities. Specific modification in the grouping of functions, subjects appearing in multiple schedules and reassignment should be considered. It should be noted that the cabinet unbundling report is not an official gazette report and hence is yet to receive Parliamentary sanction.
2. Nature of intergovernmental relations should be detailed to include clauses to provide recommendations on dispute resolution and guidelines. The roles and responsibilities of the official arbiter (courts) should be detailed, written and exemplified to avoid future conflict between any level of government.
3. Emphasis on joint control should be rendered as exemplified by Canada's water-fight structure which avoids blame game played by governments in case of conflicts.
4. The federal government should be motivated to provide framework legislations (as umbrella Acts) while the details, procedures and methods of governing should be left to the sub-national government (as in the case of Germany).
5. A commercial code encompassing one single code for transparency and accountability should be drafted to a dual advantage: to provide a common, non-discriminating framework for the entire country and to encompass all laws concerning commercial activities in the country to make it easier for investors and new entrants in various sectors.

Finally, the report also explores major post-Constitution developments in Nepal and attempts to add value to the discourse aimed at aiding implementation

as a think-tank based in Nepal. While attempt has been made to be as comprehensive as possible, there are a few limitations to the study: a core component of federal relations is impacted through fiscal arrangements as funding is a core component of all government activities. This detailed study would be explored in a Part 3 of the same series and would be published separately. Furthermore, only five sectors have been chosen while several others remain to be explored in relation to commerce. These are foreign relations and international trade, natural resource management, judiciary, among others.

PREFACE

On the eve of the promulgation of the constitution of Nepal, the then UN Secretary General, Mr. Ban-Ki-Moon noted that a constitution is a living document and urged the political leaders to act in broad national interest with continued flexibility and inclusivity. Though this reference was made with respect to the clashes among the Madhesi and Tharu communities, its application is extended to all aspects of a Nepali citizen's life; pivotal of all is the economic aspect.

Leveraging Federalism: Economic Growth and Doing Business for Prosperity is an attempt to provide for a dialogue exploring the economic angle of the federal debate. This document is prepared by the Research Team at Samriddhi Foundation over a course of several months which included research, analysis and, consultation, both formal and informal.

The report has been divided into two parts – Part 1 takes a look specifically at Federal Nepal and explores the economic history, political developments, constitutional evolution, economic capacities and the characteristics of the federal structure of Nepal. This background study provides the foundational base which helps decipher the nature and scope of different federal principles seen in Nepal. Furthermore, it also explores the future developmental plans that Nepal is heading towards and the resultant effects they would have on the Nepalese federation.

Part 2 discusses the existing literature available exploring the subject of economic governance under the new structure. Targeted focus has been given to the doing business component with a further exploratory study in regulatory aspect of banking and financial institutions, labour markets and business corporations, and sectoral review of agriculture and tourism.

A first initial draft was prepared by the team which underwent consultations from in-house senior team members followed by external consultations from more than 25 experts comprising of government officials, scholars, academicians, sectoral experts and other stakeholders. A final draft was then approved after peer review by internal and external researching.

TIMELINES

Economic Timeline of Nepal

Rana Regime	<ul style="list-style-type: none"> • Divided the country into sub-national units for administrative purpose • Military establishment • State took the ownership of mineral resources • Jagir system for civil administration was introduced
19th Century	<ul style="list-style-type: none"> • Jhara System for labour services was introduced • Four infrastructure agencies were designed – Rajya, Guthi, Birta and Kipat • Started collected revenue from the citizens by the King
(1935– 1940) AD	<ul style="list-style-type: none"> • Tejarath Adda – Started providing credit to people • Industry Council was introduced • Company Act and Nepal Rastra Bank Act was drafted • Biratnagar Jute Mill was established under Company Act • Development board for industry, trade and agriculture was established • Nepal Bank Ltd. was established under Nepal Bank Act.
1946 AD (2002 BS)	<ul style="list-style-type: none"> • Sadar Muluki Khana printed Nepali notes for the first time in Nepal
1952 AD (2008 BS)	<ul style="list-style-type: none"> • First Budget Prepared by the then Finance Minister (Subarna Shumsher)
1955 AD (2012 BS)	<ul style="list-style-type: none"> • Planning Commission was started

1956 AD (2013 BS)	<ul style="list-style-type: none"> Nepal Rastra Bank as central bank was established First 5-year plan introduced – Yojana Mandal Act
1960 AD (2016 BS)	<ul style="list-style-type: none"> Nepal Rastra Bank started printing Nepali Note Establishment of National Industrial Development Corporation
1961 AD (2017 BS)	<ul style="list-style-type: none"> Introduction of partyless Panchayat system NPC council formed under the then King.
1963 AD (2019 BS)	<ul style="list-style-type: none"> NPC dissolved and new planning body formed under chairman of council of ministers
1966 AD (2022 BS)	<ul style="list-style-type: none"> Establishment of Rastra Baniija Bank
1967 AD (2023 BS)	<ul style="list-style-type: none"> Establishment of Insurance Board
1968 AD (2024 BS)	<ul style="list-style-type: none"> Establishment of Agriculture Development Bank Taska related to national budgeting and foreign aid handed over by Ministry of Economic Planning to Finance Ministry National Planning Council morphed into National Planning Commission under the chairmanship of the Prime Minister
1970-1980 AD (2026 – 2036 BS)	<ul style="list-style-type: none"> Reconstruction of NPC as the central planning agency Exports stagnated and imports surged Country experienced severe economic crisis Adaptation of structural and economic reform programs of International Monetary Fund and World Bank – NPR devalued, import regimes liberalized, system of industrial licensing eased and simplified export procedures. Adopted regional approach in developmental planning Adopted distributive approach Priority was given to integrated rural development

1990 AD (2046 BS)	<ul style="list-style-type: none"> • Re-establishment of democracy • NPC formed again by the newly elected government
1992 – 1997 AD (2048 – 2054 BS)	<ul style="list-style-type: none"> • Implementation of 8th plan • NPC introduced free market oriented economic system for development • Government became the regulator and promoter of private investment • Tariff reduced, import restrictions abolished, duty drawback and bonded warehouse introduced • Abolished export duties and dual exchange rate • Banking sector deregulated (Commercial banks started holding foreign exchange bonds) • Industrial Enterprise Act, 1992 introduced • Introduction of National Air Policy. Foreign Exchange and Technology Transfer Act 1992 and system of Value Added Tax • Reduction of personal income tax • Nepal joined World Trade Organization and South Asia Free Trade Area. • Attention to education, health, rural drinking water, sanitation, reduction of human poverty and quality of life.
1997-2002 AD	<ul style="list-style-type: none"> • Set back in growth of industrial production • Financial progress due to establishment of bank and financial institutions • Implementation of 9th Plan • Implementation of Agricultural Perspective Plan • Adoption of more liberal and market-oriented policy • Trade, industry and tourism affected by global recession • Huge developmental expenditure growth due to Maoist conflict • Nepal-India Trade treaty

2005-2009 AD	<ul style="list-style-type: none"> • GDP per capita declined • High energy on peace accord
2015 AD	<ul style="list-style-type: none"> • Huge economic impact due to earthquake • Earthquake followed by blockade from India
2016 AD	<ul style="list-style-type: none"> • Focus on Sustainable Development Goals
2017 AD	<ul style="list-style-type: none"> • First plan of Federal Political System of Nepal

Political Timeline of Nepal

Rana Dominated King - Tribhuvan	1948 AD (2004 BS)	<ul style="list-style-type: none"> • First constitution of Nepal • Supreme Authority on all matters • Local level panchayat (Division of Power on subjects) • Fundamental Rights (assembly and peril, speech, justice, education) • International Relations monarchy dominated by Shree Panch and Shree Tin
MP Koirala Delhi Accord Rana rule ended and Shah Dynasty started	1951 AD (2009) Democracy	<ul style="list-style-type: none"> • Panchayat • Unified civil court • International Relations • Protection of investments • King has sovereign power on all matters • Child labour prohibition • Protection of cottage industries and cooperatives • Social securities

BP Koirala	1959 AD (2015 BS) Democracy	<ul style="list-style-type: none"> • Fundamental Rights (1948+equality of property and public goods) • National Language • Bicameral Parliament
	1960 AD (2017 BS)	<ul style="list-style-type: none"> • Monarch Seizes power • Constitutional and parliament • State owned media
Corruption – Panchayat BP Koirala (Last)	1962 AD (2019 BS)	<ul style="list-style-type: none"> • Monarchical Hindu kingdom • No MP democracy • Panchayat – local and national • Detailed • National language • Supreme leader king
	1980 AD	<ul style="list-style-type: none"> • Referendum (democracy vs. Panchayat) • Direct election
	1985 AD	<ul style="list-style-type: none"> • Nepali Congress – civil disobedience campaign (economic liberalization)
Gyanendra Thrown Out (KP Bhattarai)	1990 AD (2047) - 2000 Massacre	<ul style="list-style-type: none"> • Constitutional monarchy • Parliamentary Democracy • Sovereignty render • FRCP • Language, script. Culture • Directive principle • Executive government • Bicameral party • Political parties allowed inclusive government • Royal massacre • Maoist Insurgency started
	2002 AD	<ul style="list-style-type: none"> • King Dismisses government and calls off elections
	2005 AD Gyanendra	<ul style="list-style-type: none"> • King Absolute power diminishes government and declares emergency

Monarchy Abolished (Ram Baran Yadav and GP Koirala)	2006 AD	<ul style="list-style-type: none"> Peoples Movement
	2007 AD	<ul style="list-style-type: none"> Federal Democratic Republic State Competitive MP Democracy
	2012 AD	<ul style="list-style-type: none"> 1st Constitutional Assembly Fails
	2013 AD	<ul style="list-style-type: none"> 2nd Constitutional Assembly
	2015 AD	<ul style="list-style-type: none"> Earthquake and new construction

Constitutional Timeline of Nepal

1948	The first constitution of Nepal titled 'Government of Nepal Act, 1948 was effective from 1 April 1948. The constitution had 68 articles.	
1951	After the Government of Nepal Act, an interim constitution was established which restored the power to the king. This constitution was called the Interim Government of Nepal Act. The then king, Tribhuvan Bir Bikram Shah promulgated the constitution.	

Absolute Monarchy	1959	Multi-party Constitution Adapted	Parliamentary elections were conducted by king Mahendra Bir Bikram Shah. He established another constitution just before the elections.
	1960	King Mahendra seizes control and suspends parliament, constitution and party politics after Nepali Congress Party (NCP) wins elections with B. P. Koirala as premier.	King Mahendra established the Panchayat Constitution which had the provision of forming local assemblies. However, the king had the sole power in this system. Democracy was limited and no one could form political parties.
	1962	New constitution provides for non-party system of councils known as "panchayat" under which king exercises sole power.	

Multi-party politics	1980	Constitutional referendum follows agitation for reform.	
	1990	King Birendra eventually bows to pressure and agrees to new democratic constitution.	A revolt in 1990 pressurized Birendra Bir Bikram Shah to take up a new constitution and switch to constitutional monarchy. Now, the king didn't have the sole power like before. A multiparty system with parliamentary system of government was formed.
	2007	The interim constitution which was adopted on January 15, 2007, announced the abolition of monarchy. It was implemented only on May 27 2008, after the first meeting of the constituent assembly.	
Impasse over constitution	2010	The Constituent Assembly (CA) votes to extend the deadline for drafting the constitution, the first of four extensions.	
	2012	The Constituent Assembly (CA) is dissolved after failing to produce a draft constitution.	

Landmark constitution	2015	Parliament passes a landmark constitution, which defines Nepal as a secular country.	The Constitution of Nepal 2072 was endorsed on September 16, 2015 by the Constituent Assembly meeting by more than two-thirds majority. It states Nepal as a federal democratic republican nation. The executive rights of the country are stated to be belonged to the Council of Ministers while the President would be ceremonial head-of-the-state.
	2016	Government lifts fuel rationing after the ethnic minority Madhesi communities, partially backed by India, end a six-month border blockade in protest over the new constitution which they say is discriminatory.	

Part I

INTRODUCTION

Nepal has realised multifaceted economic progress as well as deterioration in its six-decade long history. The complicated economic journey has been affected by constant changes in political and governmental structures. Contemporary Nepalese economic history commences from the 1950s when most modern institutions came into existence including the Central Bank - Nepal Rastra Bank (NRB) the Central Planning Agency - Nepal Planning Commission (NPC) among others. The economic history can be studied under four distinct phases: from 1960-80s, termed as the Panchayat era, the economy was public-sector dominated through planned development controlled by the King; 1980-90 saw the initiation of outward oriented economic growth followed by economic liberalisation post 1991. Nepal recorded growth rates up to 8 percent in this period which was followed by an armed conflict by the Maoists. Although, the liberalisation agenda is still maintained post the 2000s, the momentum has met with obstacles largely due to the political instability in the country.

The economic transformation commenced with the structural adjustment and economic stabilisation programme (1985-87) due to a continuous deficit on the BoP (Balance of Payment) account in the first half of the 1980s. Earlier, Nepal was largely a state-driven economy, increasingly closed and a protectionist regime under King Mahendra⁴. The industrial investment was regulated through a rigorous licensing system, domestic industries were protected through high tariffs and licensed quantitative restrictions. However, with the restoration of multi-party democracy in 1991, economic growth accelerated in Nepal via the liberalisation policy program under the prime

⁴ King Mahendra initiated the Panchayat Era in Nepal via the Constitution of Nepal 1962

ministership of G.P. Koirala. The economy witnessed high growth rates of up to eight percent due to subsequent entry of private players in key sectors like: banking, media, industry etc.

Five years under the constitutional monarchy⁵, Nepal came under siege from the armed conflict started by Communist Party of Nepal (Maoists) on February 13, 1996. Nepal, from east to west, was affected with clashes between the Nepalese Army and the People's Liberation Army (PLA), gripping even the capital, Kathmandu, in the crossfire. It was only when Gyanendra, the last Shah King, dismissed the Parliament and took absolute control that political parties⁶ signed the Comprehensive Peace Accord (2006) declaring Nepal as a Republican State⁷. The First Constituent Assembly (CA) (2008-12), with the Communist Party of Nepal- Maoist Centre (CPN-MC) in power, failed to meet its objective and deliver a new constitution. The Second CA (2013-15) was then constituted with a dual agenda, to deliver a constitution and also act as a transition government in Nepal. They delivered the current and seventh constitution of Nepal on September 20, 2015.

The state of the economy for this period was marked by constant upheavals. The last two decades marred by constant fluctuations in the type and form of government administration⁸ affected the political establishment to realise the benefits of the 1991 reforms. This led to decades of political instability amidst confusion and lack of consensus on the arrangements of the new government structure. In a span of 26 years, Nepal saw the government headed by over 22 Prime Ministers representing the three major political forces in the country⁹. The series of events¹⁰ in the 21st century Nepalese

5 King Birendra signed the Constitution of 1991, transforming Nepal from an absolute monarchy to a constitutional monarchy with the restoration of multi-party democracy in a parliamentary format

6 Signed between the Seven Party Alliance (Nepali Congress, Nepali Congress (Democratic), Communist Party of Nepal- Unionist, Marxist, Leninist, Nepal Workers and Peasants Party, Nepal Goodwill Party (Anandi Devi), United Left Front, People's Front) and the Communist Party of Nepal – Maoists

7 Declared via Interim Constitution of Nepal 2007 (Jan 15), Enforced 2008 (May 27)

8 Government changed from an absolute monarchy to a constitutional monarchy to a republican government. Similarly, Nepal federalised into seven states from an erstwhile unitary country.

9 Nepal has three major political parties: Nepali Congress (NC), Communist Party of Nepal – Unionist, Marxist, Leninist (CPN-UML) and Communist Party of Nepal – Maoist Centre (CPN-MC)

10 See Timeline (page number)

history has further affected the economic stability of the country due to a weak architecture and left the state of affairs heavily dependent on remittances garnered through Nepalese employed abroad. These factors have strongly affected the growth of the economy and have left output at sub-optimal levels. The average growth rate of the yester-three decades stands at 4.37 percent with the highest recorded in 1994 (8.21 percent) and the lowest in 2016 (0.4 percent¹¹). The population totals to 28.96 million attributing to a Gross Domestic Product (GDP) of approximately \$682 per capita and \$730 per capita GNI in 2017. Annexure 1 encloses the trend lines for the years 1990-2017 for various economic indicators. These trend lines aptly depict the constant fluctuations in statistics affecting the health and level of activity in the economy.

At the turn of the second decade of the 21st century, Nepal emerged as a conflict-ridden country with erratic stability in its economic and political performance. Yet, it has managed to achieve certain goals which keeps the momentum. Despite its several roadblocks, Nepal has managed a rapid poverty reduction, from 42% in 1995 to 25% in 2015¹². Similarly, the primary school enrolment touched 97.12% with less than 3% children out of primary school. To a large extent, these positive changes are due to efforts of the common citizens without the aid of an effective government policy given the government instability during the transition phase.

The bulk population is concentrated within the working age bracket of 15-64 (61.7%). This demographic dividend presents itself as a strong resource at the country's disposal. These people represent the small-scale entrepreneurs, workers (domestic and foreign, across all sectors: primary, secondary and tertiary) and the increasing service sector professionals in the country. They struggle to compete in a globalised age in a largely underdeveloped Nepal. The cost of business start-up procedures amount to 24.9% of the GNI per capita. It takes a Nepalese entrepreneur about 910 days to get a contract enforced and 730 days to resolve insolvency. Only 76.3% of the population has access to electricity and a wait time of 70 days is needed to obtain a new electrical connection. The service sector is now the largest contributor to the

¹¹ Economy collapsed due to the April and May Earthquake in Nepal.

¹² Population living below the National Poverty Line; CIA World Factbook

Nepalese economy making up for more than 50% of the GDP¹³. There are only 8.86 commercial bank branches per 1,00,000 persons attributing to only 33.8% of the population who own an account at a financial institution¹⁴. These indicators point to a pitiful state in which Nepal moves through yet another political makeover. On development frontiers, Nepal is categorised as a low-income country on path for a graduation to a lower-middle income country by 2022 and plans to become a middle-income country by 2030¹⁵.

13 Inferred from the Ease of Doing Business Report 2018

14 Economic Survey of Nepal 2016

15 Nepal Planning Commission; Vision 2030; Kathmandu - 2016

DEADLINE 2022

The National Planning Commission in its 13th year plan aimed at elevating Nepal's status from a least developed country (LDC) category¹⁶. The approach paper detailed the target goals and strategies to accomplish the graduation process, that is, to upgrade the three indicators used for measurement resulting in successful graduation. This was a part of the government plan announced in the 12th periodic plan and reinforced in the 13th plan of the NPC. The approach paper to 13th Plan envisages Nepal to graduate to a developing country by 2022, though based on LDC reviews, Nepal is projected to graduate in the year 2024¹⁷.

The eligibility for graduation from the least developed category is outlined as: if, in at least two consecutive triennial reviews of prospective LDCs by the Committee for Development Policy (CDP), it complies with one of two conditions: either it meets the graduation threshold of at least two of the three LDC criteria (gross national income (GNI) per capita, the human assets index (HAI) and the economic vulnerability index (EVI)); or it reaches a level of income per capita of at least double the graduation threshold for that criterion (the 'income-only' graduation rule).

Nepal's current performance¹⁸ on the above records a marginal rise above the threshold on the HAI index, crossing the 66-index mark by two points, summing to 68.7 points. The EVI index is within the threshold limit of 32 and below, recording the same to 28.7. The triennial review concluded that Nepal is on the road to graduation, provided that it has met one of the three criterions in the triennial review of 2015¹⁹. However, it will have to meet the

16 13th Plan of Nepal Planning Commission, Government of Nepal, 2013-2016: The plan ended in 2016 and the 14th Plan was announced in April, 2017.

17 Least Developed Countries Report 2015

18 NEPAL: GNI = \$659, HAI = 68.7, EVI = 26.8, UN Development and Policy Analysis Division (Last triennial review 2015)

19 as per the Least Developed Countries Report 2015

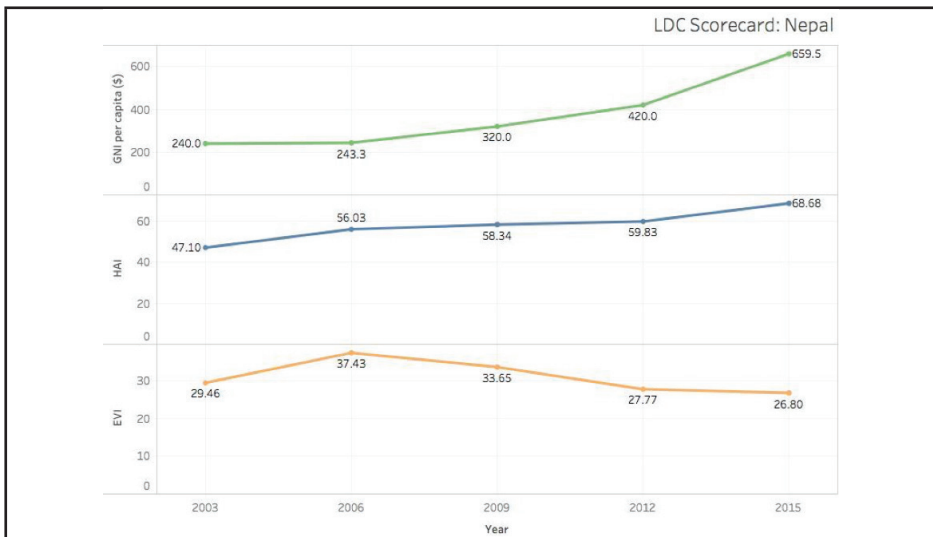
targets again in the next two triennial reviews, in 2018 and 2021, to graduate. Of the 5 countries²⁰ that met the target for the first time, Nepal is the only country which has made it to the list by improving its position on the HAI and EVI. Every other country has significantly boosted their GNI to act as a qualifier for graduation²¹. However, Nepal recorded a lower performance on its GNI index. Of the 48 low-income countries, Nepal ranks 29th on the list ranked on their GNI. The table below summarises this information and the measures that determine the LDC Status:

Table 1: Measures Determining LDC Status

REGION	EVI (Rank)	HAI (Rank)	GNI per capita (\$) (Rank)	Population (Rank)	Location
South Asia	26.8 (3)	68.7 (7)	659 (29)	27797457 (112)	Landlocked

Source: 2015 Triennial review of LDCs

Figure 1: Evaluation of LDC graduation measures (2003-2015)



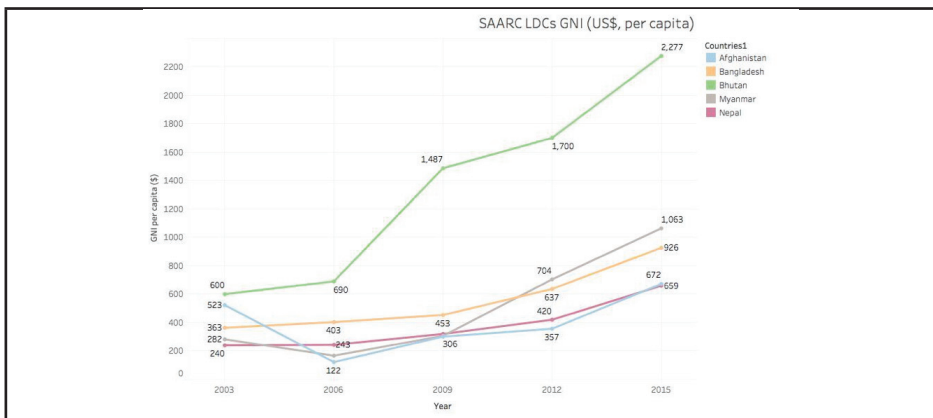
20 Bhutan, Sao Tome and Principe, Solomon Islands, Timor- Leste and Nepal

21 Timor Leste being the only country to clear the first review only by the income only qualification

Source: 2015 Triennial review of LDCs

In the South Asian region, Nepal is one of the five countries which are categorised as LDCs (others being Afghanistan, Bhutan, Bangladesh and, Myanmar²²). Amongst the South Asian Association for Regional Cooperation (SAARC) members and observer countries, Nepal ranks the lowest on the GNI as evidenced by the Figure 2. While Nepal ranks considerably high on HAI and EVI indicators, it performs abysmally on the GNI index. From further division of the GNI components, it could be verified that low GDP (which is one of the components) is potentially the cause for low GNI. The fixed currency exchange of the Nepalese Rupee (NPR) with the Indian Rupee (INR) has limited the outflow of currency outside the borders thus keeping the domestic income at home²³. On the contrary, Nepal has always been heavily dependent on remittances amounting to more than 29 percent of the GDP²⁴. Furthermore, the inflow of foreign aid heavily aids the Nepalese economy. The share of foreign assistance was recorded as Nepalese Rupee (NRs.) 212.04 billion in the first eight months of the fiscal year 2016/17. This in turn suggests that low domestic production is essentially the contributing factor to a dismal GNI figure since net-income is retained in the economy and spent mostly by the government.

Figure 2: Low-income countries in SAARC (GNI)



Source: 2015 Triennial review of LDCs

22 Myanmar is counted in the SAARC region since it occupies an observer status at the 15th summit meeting in 2008 and is a low-income country amongst all other observer countries

23 Mundell-Fleming Model: The Mundell-Fleming model has been used to argue that an economy cannot simultaneously maintain a fixed exchange rate, free capital movement, and an independent monetary policy. This is often known as the Mundell-Fleming trilemma.

24 Economic Survey of Nepal; Fiscal Year 2016/17, Ministry of Finance, GoN

The modest average growth rates achieved during the period are funded heavily from the remittances coming from foreign employment of Nepalese workers. Furthermore, the brisk rise in remittances amount to about thirty percent of the GDP wherein, one out of two Nepalese receives remittance every year. In a span of only a decade, this has contributed to a drastic reduction in poverty levels in the country, helping keep the EVI and HAI indices afloat. The graduation process, thus, is often difficult to achieve given multiple roadblocks that come forth in the process. Primary of these is the poverty trap. Low income and limited economic growth potentially pause the momentum needed for economic growth thereby entering in a perpetual cycle. As per estimates, two-third of the labour force in Nepal is employed in small agricultural holdings with chronic consequences of low labour productivity. Without modernisation through investment, the workers are unable to benefit and graduate above their current income axis (Satyal, 2010) entering into a poverty cycle. LDCs also suffer from commodity traps due to heavy reliance on production of commodities, trade for employment, income, savings and, foreign income. Coupled with rent-seeking behaviour, it prevents investment from private sectors (Adhikari, 2015) to help the economy grow. And finally, weak productive bases and limited export diversification lead to a rise in imports which further results in aid dependence and debt. Nepal suffers from an aid dependence which has not resulted in optimum economic growth due to institutional failure (Sharma, 2011). Consistent with the traps identified by the LDC Report on 'The Path to Graduation',²⁵ Nepal currently needs to ensure that it does not succumb to the above, resulting in further roadblocks for economic growth.

Apart from the susceptibility of falling into one of these traps, Nepal presents an additional challenge. Nepal is a landlocked country with no access to trade routes. In this case, it is heavily dependent on its neighbours (India and China²⁶) for support to trade. The landlocked least developing countries (LLDCs) among the LDCs generally perform considerably lower than others owing to limited export diversification, limited productive capacities, lack

²⁵ The path to graduation, Least Developed Countries Report 2016

²⁶ All trade routes are currently accessed only through India

of export competitiveness, economic remoteness and, dependence on the economic and political situations of neighbouring (transit) countries²⁷. The theory has seen translation in Nepalese history with the most recent one in 2015 whereby, the location of Nepal as a landlocked country had hindered the supply of essential goods and commodities due to political unrest. The table below compares Nepal's performance with the landlocked countries average.

Table 2: Nepal's performance with the landlocked countries average

COUNTRIES	EVI	HAI	GNI per capita (\$)
Nepal	26.8	68.7	659
LANDLOCKED AVERAGE	40.0	50.8	1518.0

Source: 2015 Triennial review of LDCs

Though Nepal has achieved its eligibility for graduation and would not be in an immediate setback not to qualify, the performance on the GNI indicators does not paint a sunny picture. The GNI per capita was \$659, during the triennial review. Though the growth rate²⁸ of the last financial year was 6.9 percent, it should be kept in mind that the figure normalises the average rate to 3 - 4 percent range²⁹, which by and large, has been the standard growth rate for more than a decade. The threshold for graduation is \$1035 and the graduation threshold for the income only category is pegged at GNI, \$2484. Thus, there is a dire need for immediate steps that fuel the economy for a sustainable economic environment.

Since there has been satisfactory performance on the HAI and EVI indices, it is important to take a closer look at the GNI. The GNI is the total domestic and foreign output claimed by residents of a country, consisting of GDP plus factor incomes earned by foreign residents, minus income earned in the domestic economy by non-residents. The net income is attributed to the

²⁷ State of Least Developed Countries Report, 2016

²⁸ Gross Domestic Product Growth Rate

²⁹ Given the growth rate recorded in the year 2015 was null due to the damage by the earthquake in April 2015

foreign income inflow in the country. Largely contributed through remittances from foreign Nepalese employment and foreign aid, the net income forms a large part of the income component. The value of remittances amounts to about one third of the GDP³⁰. The heavy dependence on remittances gives rise to lower production in the home country which does not aid any capital formation. Thus, the money is largely used for consumables that the country imports. Historically, it is evidenced that Nepal has always been a pro-remittance economy banking upon its human resource to fuel the economy (Shakya, 2013). It would be a higher value comparative advantage if, the exported human resource was a high skilled worker with a high rate of return but it is important to note that the bulk of the remittances are earned through migrant workers engaged in construction and security services, employed all over the world (Pant, 2004). It goes without saying that Nepal's comparative advantage could be its residents abroad but with the flux of the global world, solely banking upon the remittance channel comes with a high-risk factor. The recent Qatar blockade by other middle eastern countries is testament to the effects of foreign employed workers. If Nepal fails to develop its skilled workers, it could eventually succumb to a certain intensity of what is popularly known as the Dutch-disease Sapkota, 2013).

Improving the human resource takes a long-time. While the same is progressing given the increase in primary school enrolment, it is equally important to focus on the short-term targets that will help the country to prosper. Thus, it would be imperative to boost the GDP of the country. A GDP is largely the total monetary value of the total goods and services produced in a country for a fixed time period: quarterly or annually. The investment garnered mainly through the foreign loans have not seen the desired capital formation. Investment in sectors pertaining to the Nepalese economy would hold the human resource export to produce goods and services in the country that are otherwise seeking employment abroad due to a lack in Nepal. This would significantly add to capital formation in the country in terms of infrastructure, drive investment towards the social services, and also boost savings. Ex-Industry Secretary, Dr. Bholanath Chalise highlighted

³⁰ Ratio of remittances equals 29.6% (2015-16), growth of 5.3% (first eight months, 2016-17), Economic Survey 2016-17

the untapped growth potential of the demographic dividend advantage that Nepal harbours.

“The mid-nineties remained the most glorious days of Nepalese economy where Nepal was able to attain a considerably high growth rate. Following the liberalization that was initiated in the nineties, Nepal had achieved a GDP growth rate of 7.9 in years 1993-94. However, the process was not fully institutionalized. This could have been one area where the youth could have played a strong role in ensuring sustainable economic growth that would in turn also help secure civil liberties. The youth were, however, not able to show significant moral support to the process and help it institutionalize. Hence, as a result, liberalization and in turn, economic growth has remained a slow process. On the other hand, the spirit of entrepreneurship has not been as flourishing among youth (as it should be in order to influence long term economic change). “Job seeking” is still a preferred choice among the youth rather than “job creation”. Though few examples of youth entrepreneurship have been seen in the recent times, such examples need to be in huge number for actual change to occur. Unless the young and energetic forces come up with innovation in many areas and a forward-thinking attitude outside of the conventional system, their role in the larger change-making process will remain low.” (Sapkota & Chalise, 2012)

One major takeaway from the above discussion is the fact that options should be explored to increase the GNI to consistently perform for a stable economy. As the CPD sums it up,

“Thus, the goal is not graduation per se, but graduation with momentum, which will allow the development trajectory to be maintained and pitfalls to be avoided far beyond graduation: in the long term, how a country graduates is at least as important as when it graduates. This indicates a need to move beyond graduation strategies oriented to the achievement of the graduation criteria, towards “graduation-plus” strategies directed to graduation with momentum and establishment of the conditions for a viable long-term development process.”³¹

³¹ Least Developed Countries Triennial Review Report 2015, United Nations

With five years remaining to the deadline, Nepal will have to significantly step up its indicators to be able to achieve the graduation within the stipulated time period and most importantly, sustain it. The 13th year plan, designed as a three-year plan saw its culmination in the last financial year 2016-17, as the 14th plan was released by the National Planning Commission. While the 14th plan review report carefully justifies the failure of the previous plan, it is in no way different in approach and detailing out strategy to achieve the target. The 14th plan³² also lists down the reasons for under-achieving the targets set out in the 13th plan. The following reasons are identified in the document,

1. The report notes that the 13th plan did not yield optimum results on the targets set pertaining to the economic sector.
2. Political stability during the transition of the governance structure was of primary priority while the economic planning took a backseat.
3. The level of good governance lacked in all three sectors - public, private as well as the cooperative sector.
4. The catalysing effect of the instability of political authority, declining employee-employer relationship, the April 2015 earthquake and trade disruptions on the borders were the main reasons of obstruction in the industrial production as well as tourism sectors.
5. Internal production slacked which declined the value of exports setting off an imbalance in the trade deficit of the country. However, remittances saw an increase that helped neutralise the imbalance.
6. Finally, the banking sector was afloat due to the requisite foreign currency reserves.

Table 3: Comparative Review of 13th Plan (2013-2016) and 14th

32 14th Plan of the National Planning Commission 2017-20, GoN

Plan (2017-20)

Comparative Review of 13th Plan (2013-16) and 14th Plan (2017-20)					
S.No.	Indicators	Status of FY 2012/13	Targets	Status of FY 2015/16	Target
1	Annual average Economic Growth Rate	3.6	6	0.8	7.2
2	Annual average agriculture growth rate (%)	1.3	4.5	1.3	4.7
3	Annual average non-agriculture sector growth rate (%)	5	6.7	0.6	8.4
4	GDP Per Capita (In Thousands)	79.4	116.5		
5	Installed capacity of electricity generation (in MW)	758	1426	851	2301
6	Population with access to electricity (%)	67.3	87	74	87
7	Irrigation (in Hectares)	1311000	1487275	1390000	1520000
8	Total Length of road transport (km)	25133	28133		
9	Poverty			21.6	17
10	Inflation			9.5	7.5
11	Internet Penetration			44.4	65

Source: 13th and 14th plan of NPC, 2014

The approach to graduation comes with a caution. It is equally important to mark the efforts of the Nepalese people who during decades of instability in government, constant bickering amongst politicians, a civil war and even external factors like an economic blockade have managed to keep the country's economy afloat. The government's role then is to empower and strengthen the Nepalese people who have shown more backbone than any government that has survived in this country. Nepal through its Vision 2030 plans to enter the middle-income country bracket but with no concrete measures, over planning is leading the country nowhere. It has been constantly emphasized in all reports concerning the LDCs that a graduation does not mean the end of the development process. Termed as graduation with momentum, it in-fact is an indicator of reaching a milestone on the road that ultimately leads to prosperity, a quality which even the new federal constitution upholds³³.

33 Preamble, Constitution of Nepal 2015

NEPAL'S CONSTITUTIONAL HISTORY

Nepal's constitutional history dates back to 1948³⁴, following which Nepal has seen as many as seven constitutions till date, the others being 1951, 1959, 1962, 1990, 2007 and the latest in 2015. The classifying difference pertains to the structure of the State. While all previous constitutions designed the functioning of the State in a unitary mode of government, the current constitution transforms Nepal into a federal entity (also the Interim Constitution 2007).

Going through seven constitutions previously promulgated, instances of decentralization and devolution – albeit a minimum degree – can be evidenced. Even under rigid Rana and Shah regimes during which the absolute power laid with the ruler, lower tiers of governments were constitutionally recognized and were given some autonomy in certain matters pertaining to their territory (in some years if not all). It is safe to conjecture that Nepal could have transitioned into a federation much earlier (Hutt, 1991) if not for recurring political instabilities which led to sporadic changes in constitutional frameworks throughout the past sixty eight years. Finally, with the enactment of 2015³⁵ constitution, Nepal has been functioning as a federal republic³⁶. Thus, the reform marks a two-fold change, while administratively powers are divided on a federal setup between vertical orders of government elected democratically, the election of head of state also rests with the people through indirect elections. All previous constitutions thus were of a non-republic with a rigid unitary structure. However, it is crucial to note that the federalism in Nepal is still in its embryonic stage and most of the details depend on Federal laws which have not been enacted. Annexure 2 examines the comparative provisions of all Nepalese constitutions till date.

34 Promulgated April 1, 1948

35 Promulgated September 20, 2015

36 First declared through the first amendment of the 2007 Interim Constitution

Up until the recent constitution, the kings (including the central government) had assumed unlimited powers with regards to legislation along with execution of given laws; hence the extent of centralization was maximum. With the introduction of the federal constitution, concentration of power – towards the centre – has been curtailed. However, Article 232 confers the authority to issue directives and dissolve institutions (in some circumstances) on the federal government (centre); this indicates that only a moderate degree of decentralization has been established³⁷.

The constitution of 1948 in articles 16-21 recognized three levels of state legislature – district, town, and village Panchayats. They had autonomy in terms of implementation over matters concerning *“education, welfare and prosperity of the people, and the territory under their charge including justice, water supply, and basic education”* as stated by article 19. Article 67 bestowed the power to resolve disputes and interpret the constitution upon judicial committee of legislature which was semi-independent. The king³⁸ had sole command to consider and implement the list of amendments recommended by the commission in the existing structure. The commission itself was formed by the king as provided by article 68. Executive was a mix of representatives of Ranas, close members and, Panchayats who were elected; with at least two from elected legislature. Article 6 made it clear that all the authorities were subordinate to the king; thus, there was no valid reasoning in conducting an election – except for giving an illusion of superficial democracy – since everything was done as the king mandated at the end of the day. Political tussle against the Rana rulers resulted in power back to King Tribhuvan with the first instalment of a democracy in Nepal.³⁹ The following years swept away with the promise of a democratic government, the death of the king and power balance shifting to the new ruler.

37 Constitution of Nepal 2015

38 King refers to the Rana Kings w.r.t. to Preamble of 1948 Constitution wherein, the Shah King delegated all power to the Rana King

39 The Delhi Accord was signed giving power back to Tribhuvan with the help of Indian government under Jawaharlal Nehru

Under the regime of King Mahendra, the constitution of 1959 dissolved the government subunits. There was only one unit which was the nation itself. The prime minister was appointed by the king on account of having confidence of elected legislature whereas ministers were appointed on recommendation of the prime minister according to Article 13. Elections were conducted and BP Koirala became the first democratically elected prime minister of Nepal in 1959. Article 53 sub-clause (b) mandated two-thirds majority from the parliament for amendments or withdrawal of any provisions of the constitution. Although this constitution induced a more centralized system by granting concentrated power to the national government, it can be inferred from the legislative/executive relations that the power within the centre had been somewhat decentralized. However, article 57 constricted the extent of decentralization by allowing the king to appoint the members and Chief Justice of the Supreme Court, which had the sole authority over the interpretation of the constitution, Article 54. A little over a year post the promulgation of the constitution and election of the national parliament, Mahendra engineered a coup, imprisoned the democratically elected Prime Minister and took control entirely in his own hands (Mishra, 1982).

The constitution of 1962 introduced the Panchayat system. Article 30-32 divided the Panchayat into three levels – district, town, and village Panchayats though they had general purpose role only. The members of the National Panchayat were elected indirectly by the representatives of district Panchayats which comprised of the representatives of the village and town Panchayats. Article 24 extended the executive power to the king which could be either exercised directly by him or through ministers under his executive control. Supreme Court's jurisdiction extended to fundamental rights only (Article 71) and the king could unilaterally amend the constitution (Article 82). On the surface, it seemed as if there was a widespread distribution of power among different levels of government with the establishment of village, town and district Panchayats. However, on the contrary this regime witnessed a significant move of power towards the centre, more specifically in the hands of the king. As in the case of Argentina under Carlos Menem

presidency, during which “the central government devolved extensive expenditure responsibilities to provincial governments while tightening the control over revenue sources”, Panchayat regime was nothing more than a “centralization via decentralization” with central government taking substantial control over local jurisdictions. (Mihaly, 1963; Schoenfeld, 1963)

In 1967 few amendments were made to the Panchayat constitution. One of the amendments was the introduction of the post of Prime Minister and the Cabinet from national legislature although they were essentially still responsible to the king. There was a referendum in 1980, which for the first time gave a chance to the citizens to decide whether the governance structure should be based on centralized Panchayat system or should take more decentralized tone with the restoration of multi-party democracy. Panchayat system prevailed with 54.8% majority voting for the existing government structure. (Dhungel, Adhikari, Bhandari, & Murgatroyd, 1998) The amendment of the panchayat constitution post referendum introduced election of the national Panchayat directly by the people.

With the promulgation of the 1990 constitution, Nepal became a constitutional monarchy under King Birendra run by a democratically elected parliamentary government with Prime Minister Krishna Prasad Bhattarai during the drafting phase and GP Koirala post the 1991 parliamentary elections. Four levels of government existed though none of them were constitutionally empowered; Article 46 and 104 mentioned Local Authorities with no further delineation with regards to their areas of jurisdictions. The prime minister and the cabinet were appointed by the king from the legislature which commanded a majority (either majority poverty or coalition) (Article 36). Article 116 required two-thirds majority for the amendment of any articles in the constitution and the jurisdiction in relation to courts was conferred on Supreme Court which was quasi-independent (article 88) (Hutt, 1991).

The country experienced a decade long Maoist insurgency commencing in 1996, reaching its peak in the 2000s even hitting the capital (Manchanda, 2004). A series of events including untimely death of the king and several

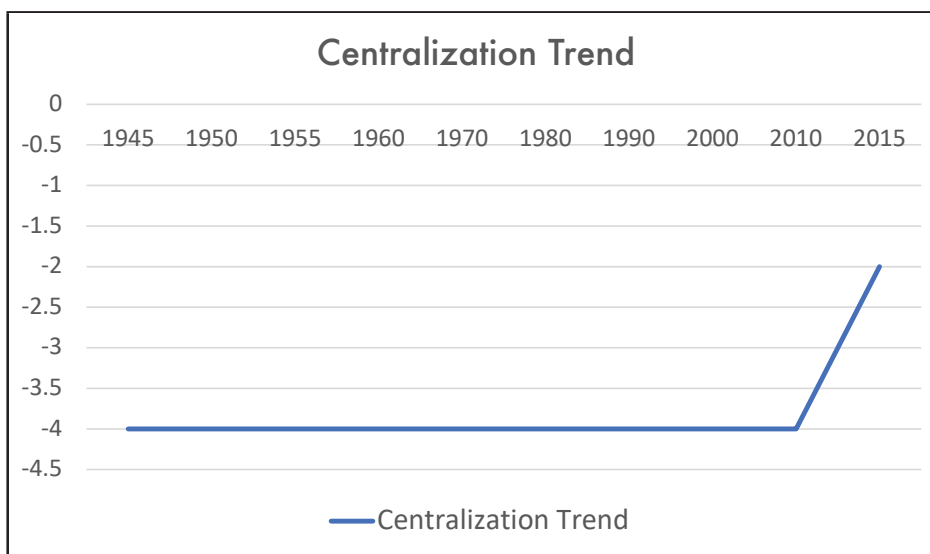
members of the royal family in a massacre, appointment of the new king, Gyanendra, and subsequent power grab by him in 2005 led the country in total chaos. A Comprehensive Peace Treaty was signed by the democratic parties (Government of Nepal) and the Maoists in 2006 which ended the war and the ruling monarchy with the promulgation of the interim constitution of 2007. The Interim constitution of 2007 laid down a foundation for the federalism by making provisions for federal system and local governance (Article 138/9). The constitution mandated the establishment of (at least) three levels of government. It took two constitutional assemblies (2008, 2013) and almost a decade again to agree on the constitutional provisions detailing the rules and guidelines by which the country would run administratively.

The Constitution of 2015 recognizes three levels of government – federal, state, and local. Part 5 and associated schedules of the constitution set out division of powers for the federal, state and local level of governments. This indicates a complete autonomy of all elected government units over their respective fields of jurisdiction as far as the constitution sanctions. Styled on the Westminster parliamentary system, the Prime Minister heads the government while the President serves as the Head of State. Council of Ministers have executive powers and are appointed by the prime minister, who also commands a majority in the House of Representatives (article 75-76). Most powers are decentralised through legislative lists in the schedules while joint competencies or concurrent powers are also established for a cooperative setup of the government.

Additional contemporary literature on the trends of constitutional history can be gathered from the following graph thus can be drawn to depict the level of centralisation of the seven constitutional forms of governments in Nepal (Breen, 2017)⁴⁰; other historical trends – autonomy, constitutionalism, bicameralism, executive legislative, basis of units, subunits, local government and asymmetry – are presented below (centralisation trend) and more in Annexure 3.

40 Sample data sourced from the cited publication

Figure 1: Centralization Trend of Nepal



Source: Breen, 2017

It is imperative to study the evolution of constitutional history in the case of Nepal as *"constitutions can be seen as independent variables, whose provisions influence the conduct of political actors by allocating authority and providing them with legally defined constraints, opportunities, and incentives"* (Simeon, 2009). The structure and division of the State power among the three tiers of government is specified in schedules 5, 6, 7, 8 and 9 and articles 57, 109, 162, 197, 214, 221, 226, 231, 232, 274, and 296 of the constitution, which outline the extent of jurisdiction each level has and respective restrictions they have to abide by. Furthermore, by allowing sub-national units to develop their own policies to meet their own needs, federalism can promote innovation and experimentation in policymaking, enabling states or provinces to pioneer innovative policies that would not be politically viable at the national level.

NEPAL'S FEDERAL STRUCTURE

"A long struggle and aspirations of people of Nepal have finally manifested into a reality."

- Ram Baran Yadav, First President of Nepal

The Nepalese Federation took its final form with the promulgation of the 2015 Constitution. This not only represented a marked change in the political architecture but also incorporated a diverse representation from various ethnic communities in the country. Federal Nepal ushers in its existence after Malaysia which turned federal in 1963. It is the most recent entry into the club of 25 federal countries which represent about 40 percent of the world population. A federal country is always unique in its characteristic features given multiple factors (geographical, historical, cultural, sociological, political, economic, constitutional etc.) which form and shape its federal identity. Nepal is a multi-cultural federation representing the various diverse groups of the country. Examples of the same are seen in Canada, Switzerland, India, Ethiopia, Belgium and Malaysia. This is contrasted with mono-cultural federations like the United States of America, Germany and Australia, which were homogenous in their populations at the time of creation.

There are some base features that all federal states in the world exhibit, a distribution of power between a central (federal) government and regional units, often called as states or provinces. Powers are divided between these orders of government who then act on their own jurisdictions with an autonomous control. However, there is no limit to nature, number and variety of regional units that could be created (Simeon, 1998). Of the 25 federal countries in the world, some exhibit a very high number of regional units, like the United States of America (50) and some are merely very few in comparison, as in Australia (6). This is exemplified by the example bore

no relation to size or population. Switzerland, with a population of just over 8 million is divided into 26 regional units or cantons⁴¹. Nepal consists of 7 regional states and 753 local governments.⁴²

The orders of government are also different in levels and nature. Most federations have constitutionally entrenched two orders of government – one at a federal level and another at a regional level. However, this is not always the case. Brazil and South Africa are examples which follow suit with Nepal by recognising three orders of government – Federal, State and Local. There are examples like that of Bosnia and Herzegovina which adopt a more complex model consisting of two entities (Croat Federation and Republic of Srpska) of which one of them is further divided into a sub-federation of three orders of government, while Belgian Federalism is studied with the concept of 3 regions and 3 communities. Nepal has constitutionally entrenched three orders of government, federal (central), regional states (provincial) and local level bodies (municipalities). The local governments are of different types namely: urban municipality, rural municipality, sub-metropolitan city and metropolitan city. By numbers, there is one federation encompassing seven regional states which further encompass 753 local governments. These local governments are further grouped together in bunches to give rise to 77 districts which function as coordination committees.⁴³

The origin of the Nepalese Federation is a product of a transition from a centralised unitary system of governance to a federal structure (Adhikari, 2011). This is in contrast with the coming together federation⁴⁴ where single states come together for the joint union of shared functions (defence, common market etc). Like Malaysia, Ethiopia, Nigeria, Spain and Belgium, Nepal restructured its government organisation to a federal one.

41 A mix of full and half cantons together make up 26 cantons in Switzerland

42 Constituency Delimitation Commission Report to the Prime Minister; Local Body Restructuring Committee. Ministry of Federal Affairs & Local Development

43 Constitution of Nepal, 2015, Government of Nepal

44 Examples include Australia, Switzerland. A hybrid mixture of coming together and holding together federations is seen in India and Canada.

However, Nepal retains a centralised character to its federal identity. A federation is termed 'centralised' on account of two reasons. Firstly, the share of revenues between the orders of government allocates a significant percentage to the central (or federal) government. On this basis, Malaysia is a centralised federation wherein, the central government retains almost 84% of the government revenue while Switzerland and Canada are the most decentralised variants with 32% and 37% revenues with the central government respectively. Nepal's federal government retains about 70% of revenues while the state and local governments are allocated 15% each⁴⁵. And secondly, a federation is adjudged to be centralised if the federal government has significant control over the sub-regional governments. In Nepal, the residual powers are held by the central (federal) government. The central government also has rights to dissolve state governments (under certain circumstances). Furthermore, several details in the constitution are largely left to be decided under federal law which gives the federal government more powers to control the activities of the sub-regional units (state and local). This is a quality, the Nepalese constitution shares with India. India is a centralised federal country; the central government has the rights to even redefine borders, create (or merge) new states, residual powers, and the power to dissolve state governments.

Nepal follows a parliamentary system of governance. A parliamentary system entails an elected legislature from which the government, headed by a Prime Minister and assisted by a council of ministers is formed. Many federations like Australia, Austria, Belgium, Canada, Germany, India, Malaysia and Spain also elect government via this system. The electoral system is a mix of directly elected representatives via the First-Past-the-Post (FPTP) method and a proportional representation for political parties at national and state levels in Nepal. Germany is a prime example that also elects the government via a direct (FPTP) and a proportional method. The table below summarises the number of elected officials at all three levels of government in Nepal. Prior to the federal structure, governments following the parliamentary system have been in place in 1959 and 1990. While the parliamentary architecture

45 Inter-governmental fiscal arrangements Act 2017

allows for a mixed representation coming from various regions of a country, they do frequently suffer from instability due to coalition politics. United States of America and several Latin-American countries follow the presidential system while, Pakistan and Russia have been cited as examples of a hybrid model consisting of both.

Table 1: Federal Government Structure

National Assembly (Rastriya Sabha): 56 Members from States (Electoral College) + 3 Members nominated by the President = 59
House of Representatives (Pratinidhi Sabha): 165 Directly Elected (FTPT) + 110 Proportional Representation (PR) = 275
Grand Total: 334
Executive: Prime Minister and Council of Ministers

Table 2: State Government Structure

State Assembly (Pradesh Sabha), Total Seven in Number			
State	FTPT	PR	Total
1	50	37	87
2	64	43	107
3	66	44	110
4	36	24	60
5	52	35	87
6	24	16	40
7	32	31	63
Executive: Governor, Chief of State, Council of Ministers			

Table 3: Local Government Structure

Ward: 1 Ward Chairman + 4 Members (2 Female + 2 General) Total Wards: 6,743 in Nepal
753 Municipalities are grouped from 7-33 wards together 753 Municipality (4 types: 460 Rural Municipality, 276 Urban Municipality, 11 Sub-metropolitan City and 6 Metropolitan City)
Executive: 753 Municipalities have [7 members (5 from Wards + Mayor + Deputy Mayor) * Number of wards in the municipality]
Legislature: 753 Municipalities have [Mayor + Deputy Mayor + Ward Presidents + Nominated (3) * Number of wards in the municipality]

BOX: SWITZERLAND'S FEDERAL COUNCIL

The Swiss cabinet, formally known as the Swiss Federal Council, formed in 1848, consists of a total of seven members. There is no single person who acts as the 'President' but it is these seven members who constitute the federal government—serving as the country's head of state and practicing the highest executive power—in Switzerland.

The Federal Council members are elected by the Federal Assembly for a term of four years. Once the Federal Assembly elects the Federal Councillor, they are not entitled to decline the election, and can neither be voted out of office by a motion of no confidence nor be impeached. Even though re-election is possible for an indefinite number of terms, the Parliament has decided to elect a sitting Councillor only twice since the beginning of 20th century.

In practice however, the Councillors serve three to five years until they decide to resign. This is the very reason why the Federal Council has been composed of the same political party for more than 60 years. The four main parties in Switzerland, through consensus, divide the seven cabinet seats based on the strength of their ballot boxes. With an equal dissemination of power and authority, each of the seven prime minister handles one department, or ministry.

The Federal Council's tasks are set out in the Federal Constitution, which entails supervising the external and internal security, transportation affairs, forestry, and water conservation. Likewise, the federal government bears responsibility for the foreign policy and customs, the monetary system, the military, and social insurance programs. It also takes steps to adjust the course of the economy and ensures uniform justice in the areas of criminal and civil law.

A unique characteristic of Switzerland's Constitution is that the sovereign power ultimately rests with its citizens, who vote on the proposed legislation several times a year at a national level.

The legislature at the federal level in most federations is bicameral⁴⁶, with the exception of Venezuela, United Arab Emirates, Comoros, Micronesia and St. Kitts and Nevis. Nepal hosts a citizen-elected lower house – House of Representatives (HoR) or Pratinidhi Sabha and an indirectly elected upper house – National Assembly (NA) or Rashtriya Sabha. This second chamber (upper house) holds an integral position in a federal country since they house members who represent the different sub-regional governments of the country. Nepal elects eight members from each of the seven states to this house, three are nominated by the President making a total of fifty-nine members in the NA.

Part 8 of the constitution defines the process of election while Part 9 lists the legislative procedures which contain the subtle differences between the functions of the two houses. Given its composition of eight members from each state, it is largely seen as a product of the new federalised setup and is a chamber for raising state issues at the national forum. The upper house has limited role when it comes to financial or 'money' bills and lacks numbers to display strength in a joint sitting vote⁴⁷. Most other federations like United States of America, India, Germany, Ethiopia, Canada, Spain, Australia etc. are bicameral with defined roles for the second house. The method of

⁴⁶ consists of two houses; a lower house and an upper house. The lower house is generally elected directly by the people while the upper house is usually selected from a mixed format of appointments and indirect elections from the constituent sub-regional governments.

⁴⁷ A joint sitting is called when a bill passed by one house fails in the other.

election determines if the second chamber is a part of an equal bicameralism or imperfect bicameralism⁴⁸. Nepal's National Assembly is an example of the latter with no special powers enshrined in the constitution.

However, it should be noted that the second chamber usually performs a check-and-balance role that is necessary to keep the dominant lower house in check. In federal countries, second chambers act as regional representations at the national level. The German Bundesrat is a prime example of the chamber acting as a regional voice on the federal level. Legislations are first tabled and approved by the only after which they move to the (lower house). has exclusive veto powers over legislation affecting state powers in Germany. Similarly, the Australian and the United States of America's Senate were founded as federal houses to represent the voice of states in Canberra and Washington respectively. However, both of these bodies soon evolved into national legislative institutions on an equal footing with their respective lower house. In other countries second chambers have special functions apart from the check-and-balance oversight function: The Indian Rajya Sabha (upper house) has special powers of initiating central intervention in state legislative fields, creation of public service commissions and approval of proclamation during an emergency imposed in the country.

The federal system divides power amongst the orders of government. This division of powers often leads to potential areas of conflict among the national and the sub-regional units in a federal country. To resolve these issues, specifically of a constitutional nature, most federations employ a constitutional court which acts as an independent umpire in cases of dispute. Nepal's dispute mechanism is envisioned through a constitutional bench under Article 137. The bench is designated to solve disputes arising between the Federation and state(s), among states, the local bodies and state(s) or, between local bodies⁴⁹. Most other federations, like Nepal, usually allocate the highest court (Supreme Court in India) or a specialised court (constitutional

48 Imperfect bicameralism is a form of bicameral legislature, in which Lower House and Upper House have different powers and functions. Because one of the two Chambers (usually the Lower House) is more relevant than the other one in the legislative process, it has more decisional power. The opposite situation, in which both Chambers have the same powers, is known as equal bicameralism.

49 Clause 2 of Article 137, Constitution of Nepal 2015

court in Germany) the authority on constitutional interpretation and disputes. The examples of Switzerland and Ethiopia stand out in this regard. In Switzerland, the ultimate sovereignty lies with its citizens, thus the citizens through their direct democracy via referendums answer cases on disputes. In Ethiopia, on the other hand, the House of Federation which is the second chamber has final authority over matters of constitutional interpretation and dispute resolution⁵⁰.

Intergovernmental relations are integral to every federal system, regardless of differences in history, geography, constitutional framework, legal culture, distribution of competences or resources, and federal design. Substantial interaction and interdependence between orders of government are increasingly unavoidable. Federal partners (or competitors) share information, determine who does, or should do, what in cases of shared competences, or clarify their respective roles in cases of exclusive ones. They extend services to their respective constituencies, create joint institutions, conclude formal agreements and battle over funding (Poirier & Saunders, 2015). Part 20 of the constitution sheds light on the intergovernmental relations between orders of government in Nepal. Article 232 mandates that the same is based on the principle of “cooperation, co-existence and coordination.” The federal government acts as the supreme body directing the state governments on matters of national importance and even dissolve them on acts that seriously undermine the sovereignty, territorial integrity, nationality, or independence of Nepal. Furthermore, the constitution via Article 234 stipulates the creation of an Inter-State Council to settle political disputes between the Federation and state(s) and between states. The coordination laws between the three orders is left to be decided by the Federal Parliament. Coordination among local bodies enclosed in a district are guided by the District Coordination Committee and District Assembly via Article 220. As noted earlier, the National Assembly may also act as a coordinating body since it comprises of members from each state.

⁵⁰ subject to legal advice from judges

Another key characteristic feature in federations is the degree of symmetry within its regional units. The Indian 'union of states' are asymmetrical due to the differences in constitutional provisions for different states⁵¹ (Kincaid, 1999). This is in sharp contrast to the United States of America where the 50 states enjoy the same degree of symmetry. Nepal, like the US exhibits symmetry of constitutional provisions across all states and all local governments. There is not a constitutionally entrenched federal district or autonomous city, though the constitution does provide a provision for the creation of one, if required through Article 56, sub-clause 5⁵². The Article 288 constitutionally designates the city of Kathmandu to be the capital of the Nepalese Federation. One could argue that politically and economically all seven states are not symmetrical in nature as they tend to represent differences in population and number of seats in national legislatures. Similarly, all seven states do not have the same resource capacity due to the vast difference in terms of their geography, access to infrastructure, current contribution to GDP etc. But under constitutional provisions, duties, and responsibilities towards their citizens, the Nepalese states are equal in power to each other.

Most federations, in addition to the three orders of government, also provide for autonomous commissions that perform several tasks where the need for a high degree of non-partisan action is required. Responsibilities of handling elections, auditing of accounts, abuse of authority etc. are applicable to all orders of the government. Part 21-28 of the constitution provide for different commissions created with a specific task they are envisioned to perform. Their legal status, roles, responsibilities and limitations are also enshrined in the constitution.

Nepal's transition from a unitary structure to a federal structure was legitimized by the first amendment to Article 138 of the interim constitution of Nepal with the words, "*democratic federal system of governance.*" *The same is reflected in the current constitution via Article 4: "federal democratic republican state."* The Federal Republic of Nepal spans over 753 local governments, seven regional state governments, and one national

51 Section 370 of the Indian Constitution creates a special provision for the State of Jammu and Kashmir

52 only for social, cultural protection or economic development

government. These divisions are guided by the federal principles of self-rule and shared rule – territorial autonomy of sub(national) units. While most federal countries have constitutionally entrenched legislative power to two orders of government, Nepal has taken a step further by introducing third tier of government into this constitutional framework. The constitution defines 35 parts with 308 articles, 9 schedules and the preamble in the beginning, which also includes provision for constitutional bodies and commissions which are autonomous in nature.

ECONOMIC PROVISIONS OF THE CONSTITUTION

The discourse on federalism in Nepal goes back over a decade with the end of the Shah dynasty in 2006. The debate has mostly centred around the issue of identity, citizenship, social inclusion amongst other related topics. Scholars have also discussed potential formats of distribution of powers, intergovernmental relations, and fiscal decentralization methods to aid in designing of the constitution for the first and second constituent assemblies (Tamang, 2014), (Hachhethu, 2014), (Chakravartty, 2014), (Sharma, 2014), (Mabuhang, 2014), (Meyerhoffer, 2014) (Urre, 2014). However, the subject of economic governance has been mildly touched in most of the above. Hence, it would be vital to go through normative economic literature on economic governance before moving to create a positive economic analysis of the provisions in the constitution. Economic governance as understood in The New Palgrave Dictionary of Economics,

"[Economic governance] consists of the processes that support economic activity and economic transactions by protecting property rights, enforcing contracts, and taking collective action to provide appropriate physical and organizational infrastructure. These processes are carried out within institutions, formal and informal. The field of economic governance studies and compares the performance of different institutions under different conditions, the evolution of these institutions, and the transitions from one set of institutions to another." (Dixit, 2008)

The definition brings in focus certain key aspects that need to be diagnosed in order to aid analysis required in the context of Nepal's federal division. They are, processes that support economic transactions while the parameters used to judge the efficiency of the above key aspects are: enforcement of contracts, collective action to provide appropriate physical and, organizational

infrastructure.

The most important phrase of the definition outlines the fact that execution of such processes takes place within formal and informal institutions. An institution is an accepted procedure that governs the process of interaction between members of society. Formal institutions would then pertain to legal entities such as parliaments, banks, or unions. Similarly, different jurisdictional levels also have different institutions. They harness powers of authority to outline the process, as described by the definition.

Another handy subset of information could also be derived from diagnosis of promulgated constitution in its reference to economic activity and regulation. The Preamble begins with '*We the people*'; without contest these words imply that the constitution belongs to the people of Nepal – a marked shift from the monarchical rule where the constitution and the government belonged to His Majesty. The preamble in its first few line recognizes the people's right to freedom. Subsequently, it envisions to end all forms of discrimination and projects Nepal to fulfil aspirations for prosperity. The preamble essentially is the introductory part of a statute or deed – constitution in this case – that states its purpose, aims and justifications.

The section on Fundamental Rights also throws some light on the rights of citizen with regards to economic governance. Article 17 – Right to Freedom – also encompasses the freedom to engage in any occupation or be engaged in employment, establish and operate industry, trade and business in any part of Nepal besides other freedoms. However, an exception to the point allows the State the exclusive right to undertake any particular industry, trade, business or service. It could be argued that this provision may come in direct contradiction with Article 44 – Right of Consumer – if the State fails to provide goods or services pertaining to the industry. Furthermore, the exclusive right of the State, in the name of common development, to belong to a centralized system, is exactly what the preamble strongly condemns.

Article 25 enables a citizen a right to property wherein he/she has the right (amongst others) to acquire business profits from his/her property.

The explanation expands the definition to include intellectual property (sub clause 6). Word of caution must be given to sub-clause 2 of the article where it would be important to note the term “public interest” – a cause of worry for constitutional experts.

Article 33 and 34 guarantee the right of employment and labour respectively. It should be noted that fundamental rights are justiciable internationally and any infringement of the same by private individuals or the State itself would be dealt by the independent judiciary. In the case of Nepal, by the constitutional bench of the Supreme Court via Article 133.

Directive Principles of State as enumerated in article 49 are guiding principles of governments of the State – federal, state, and local. Sub-clause 2 of the same article also directs the ‘State’ to implement the principles, policies, and obligations through means and resource mobilization. Although they are not justiciable in a court of law, they form an important backbone in terms of guiding the government to frame policies as per constitutional values. Furthermore, it provides the citizens with parameters to track the commitments of their elected governments to the constitution and helps them decide if the elected officials are worth their vote in the next round of elections.

Article 50 sets the tone of these guiding principles. In clauses 1 and 2, importance of rule of law and protecting the life, property, equality, and liberties of people are delineated. Clause 2 underscores, amongst others that the policies should be pro people and entrepreneurship. Clause 3 delves into economic objectives of the State wherein the State shall achieve a sustainable economic development and rapid economic growth by maximum mobilization of resources through participation and development of public and private entities as well as co-operatives to make the national economy independent. Article 51, sub-clause (b) guarantees best interest and prosperity of the people through economic, social, and cultural transformations.

Furthermore, sub-clause (d) deals extensively with policies relating to economy, industry, and commerce. A closer look into the guidelines set forth

in the constitution is relevant for this study:

Point 1: Sets forth the guidelines of enhancing national economy through people's private efforts.

Point 2: Focuses on the role of private sector to achieve economic prosperity by optimizing mobilization of available means and resources.

Point 4: Clearly identifies core conditions of the economic prosperity – fairness, accountability, and competition – in all of its activities.

Point 6: Aim for the government to diversify and expand markets.

Point 7: Directs the governments to make the national economy competitive while ending activities such as creation of black market, monopolies, artificial scarcity, and other activities that restrict competition.

Points 8,9, and 12: Aim to develop the skill and rigor of the Nepalese economy as well as to promote domestic industry by utilizing knowledge, skill, technology, and capital of the non-resident and resident Nepalese.

Points 10 and 11: Deal with principles relation to foreign capital and technological investments while maintaining transparency in these processes

Point 12: Hints at the dynamism that the governments should help create through intergovernmental relationships between different orders of the government. Emphasis is given with regards to industrial corridors, special economic zones, national projects, and projects involving foreign investment.

Article 52 reiterates and highlights the obligation of the State to make Nepal a prosperous and affluent country, without failing to protect and promote fundamental rights. Article 54 creates a monitoring agency under the federal law to review the above. Article 58 confers residual powers on the federal government; they include any subjects which are not under the responsibility of federal, state, or local levels or not stated in the constitution.

The constitution thus, is evidenced to empower people to earn their own livelihood through their property and capacity. An interference of the government (at any level), through direct or indirect means, which curtail the freedom of the Nepalese people would largely be seen as a direct attack on the constitution itself.

ECONOMIC CAPACITIES OF FEDERAL NEPAL

With the first General Elections⁵³ concluded in December, the changes in the government machinery are yet to be affected. The constitution, however, makes clear provisions on a number of roles assigned all three levels of government. Even in areas of duplicity, the constitution has provisions guiding the implementation of activities under multiple jurisdictions. At least, a theoretical framework that will shape the nature and operation of economic activities is ready on paper. As per the new State structure of Nepal⁵⁴, the country is divided into seven states (sub-regional governments⁵⁵). Historically Nepal has seen several formats of administrative divisions. Previously it was divided into 3,157 village development committees (VDCs)⁵⁶ combined into 75 districts. These districts combined in 14 administrative zones within 5 development regions which formed the Kingdom of Nepal. Now, under the federal setup, VDCs are termed as rural municipalities, districts largely remain the same with the exception of Rukum and Nawalparasi. Based on the new division of Nepal, the seven states are numbered one to seven in the east to west direction. The following indicators have been calculated using districts as common denominators.

⁵³ State and Federal elections concluded on Dec 7, 2017. Local elections were held earlier in 2017.

⁵⁴ Part 5, Constitution of Nepal (2015)

⁵⁵ Also termed as provinces, Länder (Germany)

⁵⁶ with wards as further sub-units

Table 4: Cross Section Analysis Between Seven States of Nepal

S.N.	Indicators	State 1	State 2	State 3	State 4	State 5	State 6	State 7	Nepal
1	Area (sq. Km.)	25,905	9,661	20,300	21,734	19,609	30,433	19,539	147,181
	Percent (%)	17.6	6.56	13.79	14.76	13.32	20.67	13.27	
2	Population (CBS 2011)	4,534,943	5,404,145	5,529,452	2,460,756	4,485,128	1,527,563	2,552,517	26,494,504
	Percent (%)	17.1	20.4	20.9	9.3	16.9	5.8	9.6	
3	Population Density	175.060529	559.377394	272.386798	113.221496	228.728033	50.1942957	130.637034	180.01
	GDP Percentage (UNDP-HDI 2014)	17.46	16.23	31.90	8.57	15.63	3.87	6.34	-
4	Literacy Percentage (%) (CBS- 2011)	70.71	49.67	68.19	72.78	67.00	58.37	61.54	66.60
	Male (%)	78.27	60.29	76.55	81.73	76.30	69.71	75.81	76.00
5	Female (%)	68.32	38.96	60.39	64.96	59.04	47.27	49.09	57.80
	Per Capita Income (\$)(UNDP-HDI 2014)	749.50	571.00	846.23	856.55	586.17	498.60	423.78	718.00
7	Electricity Generation (Mw)	125.64	-	354.71	447.85	21.72	3.75	8.50	962.17
8	Road Network (km/100 Km2) SSRN 2015/16 MoPIT	11.50	14.00	22.84	9.27	12.66	6.60	8.44	9.00

Source: User Calculated using multiple sources (CBS, UNFPA, NEA, DOE)

The cross-section analysis of all the seven states informs that State No. 6 is the largest with 20.67% of total land and has the lowest population density of approximately 50 persons/sq. km of land. State No. 2 is the smallest state in terms of area but with highest population density of 559 persons/sq. km of land. The population density of state 1,3,4,5 and 7 are 175, 272, 113, 228 and 130 persons/sq.km. respectively, while the country aggregate is 180. The calculated per capita income is the highest for State 4 (856.55) while State 7 has the lowest income per capita (423.78). States 1, 3 and 4 lie above the national average while 2,5,6 and 7 lie below the national average of \$718. The resources in each of these states need to be mobilised accordingly, so as to uplift the economy as well as their human resource.

Literacy always influences an economy positively as human capital is one of the most important economic resources required for achieving economic prosperity. In Nepal, State No. 4 has the highest literacy rate of 72.78% followed by State No. 1 with 70.71% literacy. Despite the fact that Kathmandu Valley is more developed than other states, the literacy rate in State No. 1 and 4 is higher than that of State No. 3. The other states considerably lag behind with most of them recording measures 70 percent. Amongst these States 2, 6 and, 7 are below the national average of 66 percent. Human capital formation is one of the pillars of the foundation of a prosperous society, thus resource capacities would now be devoted to solving the problem as per jurisdictional concerns. The literacy rate of the female population is recorded low in each of the state when compared with males. The performance of each state is not very satisfactory and thus it can be inferred that each state (especially State No. 2 and 6) needs to devote significant resources to boost its human resource capacity.

Similarly, the natural resource endowment and level of development are also varied given the differences in geographical terrain. States 1, 3, 4 and 7 have a complete north-south division, 2 and 5 are states with a larger Terai (plains) base and 6 with a larger Himal (mountainous) region. There are differences in the type of industries and sectors that each state has a comparative advantage in, given the wide spectrum of geographical,

cultural, political and economic variations.

The highest contribution of 31.90% to gross domestic product of Nepal has been contributed by State No. 3, where majority of developed cities of Nepal lies. Kathmandu Valley is considered to be the most developed in the country. State No. 2, despite being on a very low degree of development has managed to contribute 16.23% in the GDP, which exhibits the unbound capacity of the state to achieve higher development under a federal regime. However, State No. 6 is the lowest contributor of about 3.87% to the GDP. Thus, agendas and priorities would differ accordingly. Given this erratic distribution of development under the previous centralized systems, it is necessary for the states to understand their own intrinsic needs and cater to them efficiently.

Federal division of Nepal at the lowest rung is in the form of local level bodies. The Constitution of Nepal formally divides the same into the brackets of Village (Rural) and Municipal (Urban) levels. The same is vested in Parts 17-19, Articles 214-230 detailing their roles and responsibilities with respect to their legislative, executive and financial powers. Furthermore, these municipalities are grouped together to form the District Assemblies and District Coordination Committees (Article 220). In total, there are 460 village bodies and 293 municipal bodies totalling to 753 local level bodies. These 753 local level bodies are combined into 77 districts as per article 220.

The Local Governance Act 2017 further expands the structure and organization of the local bodies by categorizing municipal bodies into three divisions: municipality, sub-metropolitan city and metropolitan city. The divided numbers now spell out as 276 municipalities, 11 sub-metropolitan cities and 6 metropolitan cities. The parameters and the basis of the division is also enshrined in the Act via Section 2, clauses 3-8. Adjudged by the location of the local body with respect to Himal (Mountain region), Pahad (Hill region), Bhitri Madhesh (Inner Plains), Madhesh (Plains). These factors include the population, income, availability of civic amenities, health services, transport facilities, city roads, entertainment centres amongst others. A local body could also be deemed as a cultural or a tourist hub by the respective state governments⁵⁷. Kathmandu, through constitutional provision enjoys being the federal capital of the country (Article 288) and the right to

⁵⁷ Clause 9 of the Local Governance Act 2017

declare other autonomous region for social, cultural protection or economic development also rests with the federal government (Article 56, clause 5). For comparative reasoning and availability of data according to districts, given below is a table of district data on multiple indicators. The data is a sample collection of 151 rural municipalities, 81 urban municipalities, 5 sub-metropolitan cities and 5 metropolitan cities. The same division is also seen across different geographical terrains with 6 districts sampled from Himal and Pahad each, 2 from Inner Terai and 7 from Terai.

Table 5: District Data on Multiple Indicators

State	Muni cipality	Rural Munic ipality	GDP at Market Price	GDP (%)	Human Resource	Popu lation Density	Literacy (%)	Area	Popu lation	HDI	Per- Capita Income
State 1											
Taplejung	1	8	7448	0.54	127461	35	71.29% (79.2% male 64.1% Female)	3646	127461	0.494	813
Jhapa	8	7	44201	3.23	812650	506	75.08% (12.04% male and 68.64% female)	1606	812650	0.518	759
Morang	9	8	5678	3.93	965370	520	70.63% (78.7% male and 63.12 % female)	1855	965370	0.513	774
State 2											
Dhan usha	9	8	31453	2.3	754777	640	50.43% (60.6% male and 40.23% female)	1180	754777	0.431	580
Bara	6	9	45468	3.33	687708	1169	51.96% (62.75% male and 40.67% female)	1190	687708	0.457	916
Parsa	2	11	32852	2.4	601017	1115	55.9% (66.9% male and 43.8% female)	1353	601017	0.464	757

State 3											
Kathmandu	11		215391	15.76%	1744240	3467	86.252 (92.17% male and 79.76% female)	395	1744240	0.632	1710
Dhading	2	11	14662	1.07%	336067	260	62.858 (71.079% male and 55.699% female)	1926	336067	0.461	607
Chitwan	6	1	39713		579984	541	76.98 (83.867% male and 70.677% female)	2218	579984	0.551	951
State 4											
Kaski	1	4	34210	2.50%	492098	463	82.375 (90.101% male and 75.354% female)	2017	492098	0.576	966
Gorkha	2	9	12503	0.91%	271061	252	66.338 (75.09% male and 59.436% female)	3610	271061	0.481	643
Tanahun	4	6	15336	1.12%	323288	435	74.826 (83.678% male and 67.93% female)	1546	323288	0.506	663
State 5											
Rupandehi	6	10	43948	3.22%	880196	1268	69.783 (79.221% male and 60.785% female)	1360	880196	0.498	695
Rolpa	1	9	6327	0.46%	224506	185	60.004 (71.548% male and 50.481% female)	1879	224506	0.395	398

Pyuthan	2	7	6779	0.50%	228102	140	67.012 (78.184% male and 58.634% female)	1309	228102	0.413	421
State 6											
Surkhet	5	4	14151	1.04%	350804	455	73.116 (82.04% male and 64.916% female)	2451	350804	0.476	563
Jumla	1	7	4900	0.36%	108921	125	54.656 (68.241% male and 40.843% female)	2531	108921	0.409	623
Dolpa	2	7	1706	0.12%	36700	21	54.148 (67.863% male and 40.618% female)	7889	36700	0.401	643
State 7											
Doti	2	7	7216	0.53%	211746	164	56.347 (73.409% male and 42.338% female)	2025	211746	0.407	479
Kailali	7	6	32376	2.37%	775709	787	66.318 (76.157% male and 57.051% female)	3235	775709	0.46	583
Bajura	4	9	3122	0.23%	134921	197	55.682 (68.842% male and 43.327% female)	2188	134912	0.364	324

Source: Author's calculation on the basis of multiple sources

Part II

LITERATURE REVIEW

"The reason why a division of power between different authorities always reduces the power that anybody can exercise is not always well understood. It is not merely that the separate authorities will, through mutual jealousy, prevent one another from exceeding their authority. More important is the fact that certain types of coercion require the joint and co-ordinated use of different powers or the employment of several means, and, if these means are in separate hands, nobody can exercise those types of coercion. The most familiar illustration is provided by many kinds of economic control which can be effective only if the authority exercising them can also control the movement of men and goods across the frontiers of its territory. If it lacks that power, though it has the power to control internal events, it cannot pursue policies that require the joint use of both. Federal government is thus in a very definite sense limited government."

-Frederic Von Hayek, Constitution of Liberty, 1960

The Nepalese polity as of today has metamorphosed from a simple, centralised, hierarchal structure to one seen as a compound and mixed form of government. Constitutionally entrenched orders of government (federal, state and local) with an autonomous character have powers assigned (legislative, executive or, both) to them (Riker, 1964). This change fundamentally affects how institutions, both formal and informal, need to reorganise this allocation to be able to achieve the aspirations envisioned in the federal constitution.

The federal variation seen across the globe as well as in intellectual discourse conclude that there is not just a singular model of a federal country. The factors contributing towards the adoption of a federation are thus diverse; geographical, ethnic, economic, political, historical, constitutional etc. Specifically, for Nepal, the debate has largely centred around identity.

The Comprehensive Peace Agreement, signed in 2006, initiated the peace building process in the country after the end of the constitutional monarchy. The result was the adoption of the federal structure via the Interim Constitution, 2007. The promulgation of the constitution in 2015 lays down a framework and structure for federal Nepal but further details were left to future deliberations. Thus, it is imperative to study existing literature and chart out a roadmap for federal Nepal. This paper attempts to do so in the economic context by exploring division of competencies⁵⁸ to foster economic growth via domestic private enterprises.

The change in government structure, though inspired by non-economic reasons, is coherent with the economic argument for the division of powers between orders of governments as centralised governments do not possess sufficient information or knowledge to tailor policies to the citizenry spread across a nation (Hayek, 1945). This in turn suggests that governments closest to their constituents would be best suited to cater to the demands of people. Because lower governments have better information about projects, policies, and citizen preferences, they will make better decisions about policies with a local impact.

In Nepal, the jurisdiction closest to the citizenry are the local bodies. However, some national public goods are common to the entire country, for example defence, and hence need to be catered by a higher order of government. The guiding principle of the economic theory of federalism is thus to assign the policy responsibility to the smallest order of government that can accomplish the task (Oates, 1972). The principle is also best known as the decentralisation theorem or as the principle of subsidiarity, endorsed by the United Nations Development Programme's (UNDP) 1999 Report on Decentralisation:

“Decentralization, or decentralising governance, refers to the restructuring or reorganisation of authority so that there is a system of co-responsibility

⁵⁸ Powers or functions assigned to each order of government

between institutions of governance at the central, regional and local levels according to the principle of subsidiarity, thus increasing the overall quality and effectiveness of the system of governance, while increasing the authority and capacities of sub-national levels."

Apart from the above-mentioned feature, additional economic benefits are associated with a federal structure of government. A federal system creates multiple sub-national governments. These jurisdictions allow the freedom of choice to residents to choose the preferred system of governance they like. This essentially creates a positive competitive environment whereby political officials are forced to compete for efficiency in their supply and regulatory practices. This also leads to an optimal mix of policies across jurisdictions which differ depending on the demands of the citizenry of that particular jurisdiction (Tiebout, 1961). Adding to the line of thought, Buchanan notes:

"The principle of federalism emerges directly from the market analogy. The politicized sphere of activity, in itself, may be arranged or organized so as to allow for the workings of competition, which is the flip side of the availability of exit, to become operative. The domain of authority for the central government, which we assume here is coincident in territory and membership with the economic exchange nexus, may be severely limited, while remaining political authority is residually assigned to the several "state" units, each of which is smaller in territory and membership than the economy. Under such a federalized political structure, persons, singly and/or in groups, would be guaranteed the liberties of trade, investment, and migration across the inclusive area of the economy. Analogously to the market, persons retain an exit option." (Buchanan, 1995)

Federalism and subsequent decentralization lead to a higher innovative capacity of the political system. Federalism offers the advantage to test out policies on a smaller scale to study the consequences before testing them on a nation-wide scale (Oates, 1999). This 'laboratory federalism' allows sub-national governments not only to try varied policy practises within their jurisdictions but also develops a firm ground for upcoming politicians to be

put to test before they are entrusted with national responsibilities. Given the unending political instability in Nepal, federalism may offer a solution to both problems—political and economic, if implemented in spirit.

Federalism is also argued to improve private sector economic performance. Assigning tax and regulatory responsibilities to state and local governments checks governments' temptation to exploit business investment through confiscatory capital taxes or excessive business regulation (Weingast, 1995). The private sector directly helps enterprise growth and development amongst the citizens offering them a chance to unleash their true potential. As concluded by Inman, decentralised governance does have a unique contribution to make to a society's ability to enforce property rights, to protect political and civil rights, and then because of such right protections, to enhance private sector economic performance. (Inman, 2008). As previously cited, Sapkota and Chalise (2012) have spoken at length on the entrepreneurial potential of the Nepalese youth. In light of the same, Barry Weingast builds upon Riker's general characteristics of federalism to advocate for a market preserving federalism;

"A federal system is market-preserving if it has three additional characteristics: (F3) subnational governments have primary regulatory responsibility over the economy; (F4) a common market is ensured, preventing the lower governments from using their regulatory authority to erect trade barriers against the goods and services from other political units; and (F5) the lower governments face a hard budget constraint, that is, they have neither the ability to print money nor the access to unlimited credit. This condition is not met if the central government bails out the lower one whenever the latter faces fiscal problems." (Weingast, 1995).

From a political economy perspective, fiscal competition is interpreted as a possibility to reduce the size of government and thus to maintain the efficiency of a market system. Because of enhanced migration possibilities of mobile investors, governments of sub-federal jurisdictions are forced to tailor their fiscal policies to the needs of investors and to find policy solutions

favouring market economies (Brennan and Buchanan 1980). Similarly, factors that affect economic growth have also been studied within the ambit of Federalism studies. For governance, it is seen as a disciplinary tool that keeps a check on governments thereby moving towards an efficient system (Shleifer & Vishny, 1993).

While all the above assessments come up with a fixed set of assumptions, the ultimate outcome of the federalising process depends on multiple factors. As put forth by Robert P. Inman and Daniel L. Rubinfeld, “the choice of an ‘optimal’ level of decentralization depends on the relative importance one places upon economic efficiency and the potentially competing values of political participation, economic fairness, and personal rights and liberties.” (Inman & Rubinfeld, 2017)

Inman and Rubinfeld (2017) also note, the economics of federalism views the primary task of government as solving the failures of private markets to satisfy the demands of citizens for goods and services and the economic task for federalism is to provide a means to solve these market failures. For goods and services for which congestion becomes evident within relatively small populations, and where the spatial reach of any externalities is modest, economic federalism recommends using small local governments.

The discourse on the economic efficiency of federalism process also has a number of critiques, given the density of the subject and its application across the world. Bewley states that intergovernmental competition limits inefficiencies as advocated by Tiebout but may not completely eliminate them. Similarly, Susan Rose Ackerman addresses concerns of excessive local government corruption deterring economic growth.

Similarly, empirical evidences are also contrary with respect to federalism and economic growth. Papers by Yilmaz (1999), Lin and Liu (2000), Akai and Sakata (2002), Thiessen (2003), Stansel (2005) and Iimi (2005) all find a positive relationship between decentralization and economic growth. On the other hand, works by Davoodi and Zou (1998), Zhang and Zou (1998),

Woller and Phillips (1998), and Xie et al. (1999) disconfirm the conjecture by finding a zero or negative connection between fiscal decentralization and growth. Recent work by Brueckner has shown that federalism, “which allows public-good levels to be tailored to suit the differing demands of young and old consumers, who live in different jurisdictions, increases the incentive to save. This stronger incentive in turn leads to an increase in investment in human capital, and a by-product of this higher investment is faster economic growth” (Brueckner, 2006). Empirical studies in relation to the levels of corruption have also seen some positive results (Fisman and Gatti, 2002, Adesera et al. 2003). In the context of Nepal, Devkota (2013, 2014) studied the effect of fiscal decentralisation on economic growth and found a positive co-relation between the two, thus proving that one enhances the other (Devkota, 2013, 2014)

The economic agenda for Nepal is one of crucial importance. While the national calendar sets the country 57 years ahead of the world, in reality, the economy of Nepal seems to be moving on a retrograde motion. The constitution envisions a free and prosperous Nepal but the reality greatly depends on the corrective measures taken in the right direction to achieve that target. As noted, institutions on the other hand can be designed and/or changed to meet the unique needs of a diverse (or homogenous) citizenry. Thus, one critical way in which researchers and policy-makers can assist diverse national and international governments with better governance is to encourage institutions that have worked well for similar countries in the past (Charron, 2009)

APPROACH

The economic federalism literature proposes several advantages of dividing taxation and expenditure authority as well as policy formulation allocation across levels of government. Local governments are assumed to have an information advantage in identifying local needs. Decentralization additionally allows for more variety in the provision of public goods so that local preferences can be satisfied. Mobility ensures efficient matching of citizens with jurisdictions that provide the public goods they prefer. And lastly, local governments are also potential laboratories for policy experiments.

In the book, *The Economic Constitution of Federal States*, Breton and Scott have defined a methodology to study the different competencies and their relation to different variables that effect the economic performance and development of a federal State (Breton and Scott, 1978). Furthermore, they also define a formula to evaluate the degree of centralisation and propose models for an efficient federal State. While the calculations and models cannot be studied as of now, given Nepal's federal structure, aged only 2 years, the approach could be adopted to give us a structure to study comparative conclusions from international experiences.

Federalism as a governance structure has existed for over 200 years with the United States of America adopting the federal structure in the year 1789. Fast forward to 2018, Nepal is the youngest federal republic in the world with the promulgation of the constitution in 2015. There are 25 federal countries, encompassing more than 40% of the world's population, with numerous other exhibiting federal features through excessive decentralisation of powers to sub-regional units. While this paper was being researched upon, another Southeast Asian nation, the Philippines was debating about the nature of federalism they want to adopt. The European Union in itself is

quoted as an example of a federal structure. Needless to add, the fast pace of transformation in the cultural, social, political and economic spheres all over the world has led to federal systems constantly adapting to assimilate and accommodate these changes to overcome the challenges of the day.

As noted by several scholars, the experiences of other federations aid the process to foresee the likely consequences of a particular arrangement. Both positive and negative examples have been instrumental in adding the rigour and depth to constructively reinvent federal structures to deliver the promises of federalism (Wibbels, 2005).

An important note at this juncture would be to be constantly reminded that there does not exist a single model of federalism. The arrangements adopted by federal states are often unique and intrinsic and hence its arrangements are greatly influenced by a number of factors. However, our main aim is to study the provisions which govern the economy of a country, the structure of which is largely attributed to a calculative science rather than that of a rhetoric. The same is conducted through a cross-examination of the characteristics of the five classes of functions or powers that are assigned to the various jurisdictional levels that constitute the public sector of a given society.

Where,

a function refers to the power, responsibility, and authority that the government of a jurisdiction possesses to make decisions, to pursue policies, and to undertake activities in a particular area or in a specified domain once that power, responsibility, and authority has been assigned or given to a particular jurisdictional level (not to a jurisdiction per se, except in the case of the national jurisdiction when the jurisdictional level and the jurisdiction are co-terminus)

The assignment of a function to a jurisdictional level is therefore a necessary condition for the governments of the jurisdictions at that level to have power to make decisions on the matters pertaining to that function. Indeed, once

a function has been assigned to a jurisdictional level, governments of jurisdictions at that level are free to make their own decisions about the quantity and character of their activities under that power, which includes, of course, the option of taking no action. These decisions are defined as policies.

These functions as per a general economic classification are divided into five broad categories namely,

a) regulatory functions

Regulatory functions encompass policies and decisions that assist, direct, guide, and govern the production, exchange, and distribution of goods in the private sector, as well as the administration of justice, civil rights, free speech, etc. It should be noted that, policies that can be implemented if the power or responsibility has been conferred on a government by the assignment of the particular regulatory function.

b) supply functions

Functions are also assigned which enable public expenditures on certain goods and services. They include expenditures on the armed forces, on lighthouses, education, public schools, hospitals, and street cleaning - to name but a few. This would include goods and services which may or may not be provided by the private sector – banks, shops, media houses etc.

c) revenue functions

The revenue functions is the power to command not only the collection of monetary revenues or taxes, but also the direct levy of goods and services. One can classify taxes according to their base: it is possible, for example, to distinguish between taxes on profits, on personal incomes, on payrolls, on sales, on property, on inheritances, and on other bases. If one operates with this distinction, then the right to use the income base is a function, while what we call policy concerns the details of rate, exemption, time of payment, enforcement, and so forth.

The revenue functions also include the power or right to impose fines, to draft individuals for the armed forces, or to fight forest fires, or for some other special purpose task forces. It also includes the right of expropriation, forcing private owners of property to sell. In these special cases, the 'revenue' that accrues to the state is the net value of the goods, services, or assets 'commandeered.'

d) fiscal redistributive functions

It refers to an intention to change the distribution of income or wealth among a group of persons, or in favour of a group of recipients, the formula that defines the equalisation factor to redistribute revenue between jurisdictions, typically from the national to sub-regional units.

e) stabilisation, of macro-aggregate dimensions of the economy, functions

The stabilization functions relate to the power to engage in certain actions with the intention of stabilizing any number of aggregate magnitudes, such as the level of output, the level of employment, the level of prices, etc. as well as the rate of change in these aggregate magnitudes. Though stabilization functions are defined by intent with respect to macro-dimensions, the instruments used by governments are certainly not restricted to any textbook list of macro-economic policy instruments; some micro-economic instruments can also be employed.

Using an assignment table, we individually create a matrix of a number of column functions that pertain to economic governance and highlight the jurisdiction to which the function is assigned. This is sourced through legislative lists, constitutional articles or framework legislation. Once the assignment of functions is established, trends are observed in comparison with the assignment of functions as per the Nepalese constitution. Further inquiry is conducted to inform the framework of the regulation and the governance structure corresponding to the particular function as well as the country. The same is studied on two levels, legislative power and executive power. This gives a blended approach of studying the vertical and horizontal

separation of power in the federations.

Though the total number of federations is 25, we take a concentration of 13 countries including Nepal for our analysis. This is due to limitation of information, differences in size, population and, sovereign status as well as to narrow conclusions. The pool of countries selected are spread over the world, belong to different categorisations (developed, developing, least developed), similarities in ethnographic-linguistic diversity, etc. thus making an attempt to study a broad sample.

The federal states studied are;

Developed Countries: [5] Switzerland, Germany, Canada, United States of America and Australia

Developing Countries: [6] Brazil, Mexico, Malaysia, India, South Africa, and, Nigeria

Least Developed: [2] Ethiopia, Nepal

The countries pertain to different continents, thus tend to touch examples from all over the globe;

Asia:	India, Nepal, Malaysia
Europe:	Switzerland, Germany
Africa:	Nigeria, South Africa, Ethiopia
South America:	Mexico, Brazil
North America:	Canada, Unites States of America
Australia:	Australia

The countries also exhibit a variation in the society composition—homogenous versus heterogeneous. The sample was thus chosen to effectively represent a balanced perspective. A comparative analysis on several indicators of economic growth and nature of the federal states is reviewed in Annexure 4.

ALLOCATION OF FUNCTIONS

Supply and regulatory functions are studied together under the heading of 'allocation functions' (BRETON & SCOTT, 1978). It should be noted that the variation in the scope of power distribution and responsibilities are vastly different. Thus, rather than suggesting a single pure model for distribution, several practical variations are studied within the common framework of federal systems (Majeed, 2006).

These powers over allocation functions are bound to affect governance and hence, economic development in almost all policy areas. As noted by scholars, countries have also shown both a positive trend towards centralisation of power (as in USA, Australia) while other countries have seen a step towards further decentralisation of power (as in India, Canada). Thus, based on the degree of centralisation, most federations could be represented on a spectrum.

Division of power is a central feature of federations. It is the defining characteristic that distinguishes federation from other political systems. There is a constitutionally guaranteed division of power between the government of the whole country and the regional governments. Federations are therefore distinguished by the formal constitutional distribution of legislative and administrative functions including fiscal power.

The list of functions we examine are:

Labour Market: Labour Laws, Skill Development and Trade Unions

Banking and Financial Institutions: BFIs

Tourism Sector

Agriculture Sector

Business Enterprises: Micro, Small, Medium and Large Enterprises

Certain aspects should be kept in mind;

Political power is divided and allocated between the federal government and the constituent units and both operate autonomously within their own jurisdiction. Division of power is directly related with the design of a federation. The federal government, as the general government of the whole country, is entrusted with powers that are of concern for the federation. The sub-national governments⁵⁹ are sovereign as far as powers assigned to them in the constitution. Neither the federal government nor the sub-national governments can interfere in the power of the other. Each level of government is legally independent of the other. The sub-national governments can exercise only those powers assigned to them in the federal constitution. The federal government cannot interfere in the sphere of jurisdiction allocated to the sub-national governments.

Federations are an outcome of bargains at a particular time with the view to serve generations and written constitutions are evidences of the records of the terms of the bargain. *“The particular purpose of constitutions in federal systems is to spell out as precisely as possible how the powers are allocated to different levels of government and the procedures to be followed for these allocations to be altered.”*

The distribution of power must be spelt out in a written constitution and cannot be undertaken orally. All of the federations under consideration have written constitutions. Not only are federations based on written constitution, but they are based on a supreme constitution as well. The constitution is the source of authority of the multiple levels of governments and therefore logically must be supreme. The constitution should be supreme as it is the source of the authority and as it also regulates the relation between the multi-tiered governments.

For Nepal, the allocation of functions pertaining to the three orders of government are enumerated in Schedules 5-9. Schedule 5 lists competencies

⁵⁹ State and Local

that pertain to Federal domain, 6 lists State powers, 8 lists Local level power. Lists 7 and 9 are concurrent or joint competencies between Federation and State and all three orders (federal, state and, local) respectively. Annexure 5 lists down all functions within the scope these five lists as per the Constitution of Nepal.

GENERAL OBSERVATIONS

The constitutional entrenchment of vertical power sharing in terms of legislative and executive forms the bedrock of the federal model. Through the 200 years of federal history, numerous scholars have presented arguments, debates and discourses on the federal idea of power sharing. The power sharing lies in two important domains, an exclusive power assigned to a jurisdiction and in terms of a shared power between several jurisdictions. The shared power, termed concurrent power embodies the shared rule that a general federal structure encompasses (Elazar, 1987). In a federal system of government, sovereignty is shared and powers divided between two or more levels of government each of which enjoys a direct relationship with the people. Nepal's constitution divides power in both formats in a three-tier structure: federal, states and local level.

It is widely accepted that no two federations are alike, given variations in historical context, geographical variety, economic prowess, security, demographics, linguistic and ethnic, intellectual capacities, time-period and international factors. Thus, there by no means, exists a federal structure which is ideal and is one fit size for all. Rather, it is a collection of certain principles which when adhered to, make a federal system of its own unique importance. Nepal fares differently than the rest of the world under these theoretical concepts which form the trunk of the federal structure. These are the historical evolution of the structure, symmetry, intergovernmental relations, competition among states and degree of centralisation (or non-centralisation)

The differences are also affected by political execution, behaviour and processes. This forms a significant portion of the debate since political actors are direct stakeholders in the process which work towards or against the tenets

of the federal structure. These also play a major role in intergovernmental relations between the different jurisdictions since a majority of powers also lie within the purview of concurrent or joint competencies.

In the sample we analysed, some broad conclusions on the federal development of Nepal becomes apparent. It is well established that Nepal belongs to the category of federations carved out of a previously unitary state. What is unique in Nepal's case is an absence of a colonial power or external authority controlling affairs of the state. Previously a monarchy, Nepal has flirted with democracy on multiple occasions, all of which turned into a failure. These factors in conjunction with an armed rebellion lasting a decade have risen the political instability in the country to a higher magnitude.

Generally, it is observed that federal powers tend to be stronger when there are homogenous social characteristics. Switzerland, United States are examples of diverse social characteristics. On a lighter note, while comparing it should be accounted for that both these federations lay their origins in the 18th and 19th centuries. Their constitutions display a very generic format when it comes to discussion on distribution of powers. For Nepal, it could be argued that while Prithvi Narayan Shah was unifying the country, it could have developed as a similar model. But the transformation to a repressive and redundant style of government under the monarch unified the country to a strong Kathmandu-based hierarchy.

In the current format, territorial diversity has chances to lead to fragmentation and hence, a strong federal balance has been the norm. The same is witnessed in Spain, India, Belgium etc. Though Nepal is characterised by a strong ethnic divide across geographical regions, similarities, especially with the use of Nepali language are forms of homogeneity in the country. The same has diluted powers to the sub-national units but in essence is adjudged to be a centralised federal structure, wherein the federal government does have a strong part to play. Brazil, Mexico and Nigeria have had authoritarian regimes because of which the federal structure they exhibit is strongly centralised.

While diagnosing Nepal in the scheme of things, the country takes a mixture of all these different trends thus becoming a complex model in its

establishment. While most federations constitutionally entrench two orders of government (USA, Canada, Australia, Belgium and Spain), some like Nepal, make provisions for three (Brazil, Germany, India, Mexico, Nigeria and Switzerland). But again, the strength or power of these local governments varies from federation to federation. While Canada and Switzerland have very strong local units, Malaysia has very weak local units. India, through a constitutional amendment in the 1990's did create a third tier but it has been largely left to the states to facilitate the action, with no positive change. Switzerland on the other hand enjoys stronger power sharing for the local level governments.

The variations in degrees of centralisation give rise to different forms of the governance character: legislative, executive, administrative and financial. Nepal follows the Westminster style i.e. a parliamentary democracy wherein, the legislature and executive arise from the same elected officials. This form of relationship does have some advantages to its name;

- It reinforces the autonomy entrenched for the sub-national units through their legislative bodies,
- the legislative body has the authority to implement its own legislation and,
- parliamentary systems make the executive branch accountable to the legislature, which is directly elected by the people.

These characteristics are similar in Canada, Australia, India etc. Germany and Switzerland are compound formats, wherein the legislature is heavily centralised and the execution/ administration is heavily decentralised (non-centralised). Thus, while comparing individual assignment of powers, caution is maintained to check both the legislative and executive powers.

Symmetrical nature of Nepali constitution assigns an equal status of 'statehood,' though there is a provision to create federal territories or autonomous territories. On a general trend, it has been recorded that asymmetrical distribution tends to fuel problems, as seen in Jammu and Kashmir, and North-eastern States of India, Quebec in Canada and more

recently Catalonia in Spain.

One of the bigger issues to address at this juncture is Part 20: Interrelations between Federation, State and Local Level. It clearly specifies the nature of the federation to be that of a 'co-operative' nature. While delving further on the text of the constitution in Parts 7,14 and,17, it is clear that the executive powers are shared between all jurisdictions pertaining to the lists that they cater to;

- No specific schedule numbers are mentioned in Federal Executive but the text clearly applies to all schedules i.e. 5,6,7,8 and,9.
- Schedule 6,7 and 9, with State and,
- Schedule 8,9 with Local.

The nature of Nepali politics, to the extent, the drafting and passage of the Constitution has long been one of a political bargain between political parties. Hence, given the reality, the co-operative nature of this feat requires a very strong judicial oversight. It is not unknown that the judicial process of Nepal is not one to be relied upon strongly. Blame game from one administration to another can be easily predicted given multiple instances of Nepalese governments of various types continuously fighting, fragmenting, cementing again in the past with no apparent benefit to the people.

This co-operative nature comes in the form of concurrent powers. Schedules 7 and 9 deal with joint competencies at Federation-State and Federation-State-Local respectively. Concurrency allows states to act on their own interest until and unless a national federal action is required. For Nepal, the main reason for creating a federal government was because the Singha Durbar government proved inefficient in catering to the needs of the people. Hence, simply relying on good intentions may not prove to be a feasible outlook going forward.

Federalism also provides for a competitive advantage, for which, a competitive set-up, whereby sub-national governments enjoy exclusive powers from the federation to build their own capacities. These sub-national governments try

different techniques to recognise the best practices in a given policy direction and help benefit the entire country. There are two broad advantages for creating a competitive and exclusive distribution of power;

- It reinforces the autonomy of the particular government, thus avoiding the blame game from one administration to another and,
- it clearly determines which government is responsible and accountable for policy in the jurisdiction. This enables the citizens to judge their governments wisely and choose suitable candidates through informed choice.

However, a concurrent power is required and cannot be done away with. Given the sample of countries studied, the concept of “framework legislation” answers the questions. The Federal governments provide a broad conceptual framework legislation to be applied to maintain standards and quality in policy, and sub-national units then draft rules and procedures to adapt the framework according to their needs and requirements. Germany enshrines the same in their constitution and many others like Mexico and Brazil do imply it in their respective constitutions. While no such consideration is available in Nepal’s case, it should be well be taken as a method of improvement.

Scholarly work pre-promulgation of the constitution was aimed at aiding the Constituent Assembly, specifically the Committee on State Restructuring and Division of State Power (CSRDSP) for power sharing in federal Nepal. Several others provided literary analysis on the provisions and international experiences of other countries. Based on our distribution of the assignment table constructed and inferred in the previous chapter⁶⁰, the following section provides each assignment function in context of Nepal with respective commentaries;

⁶⁰ The same can be accessed from the Samriddhi Foundation’s official website.

SECTOR SPECIFIC OBSERVATIONS

BANKING and FINANCIAL INSTITUTIONS

The core health of an economy is largely synonymous with the health and robustness of its financial sector. Therefore, banks and financial institutions form a central feature of this active participation. Nepal's banking evolution took place after the creation of Nepal Rastra Bank in 1956⁶¹, following which government-controlled banking operations improved access to financial services and reach among the Nepalese population. The current phase of the banking sector is post 2002 changes which has significantly adapted to the modern banking sector reforms in line with international standards, though the same has been set at an evolving stage. Currently, there are 209 banking and financial institutions including licensed cooperatives and chartered non-governmental organisations with banking facilities. Access to finance, though growing, is still marked with low access as per indicators (Economic Survey, 2017).

The division of power, as per the constitution, allocated the federal level to regulate "Central planning, central bank, finance policies, monetary and banking, monetary policies, foreign grants, aid and loans" while the States have been allocated the power which reads, "Operation of banks and financial institutions in accordance with the policies of Nepal Rastra Bank, cooperative institutions, foreign grants and assistance with the consent of the Centre."

Though it does seem that the power is shared by these two jurisdictions but in constitutional terms they are written as exclusive powers of the federal and

⁶¹ Though Nepal Bank was established in 1937, it was a commercial bank and was not a regulatory body.

state respectively. This largely means that the jurisdictional authorities do not have an over-riding veto power in terms of a conflict. The Cabinet Unbundling report additionally dissects these points to serve as explanations but the same does not divide the work marking “Policy, Law, Criteria, Coordination and Regulation related to banks and financial institutions” under the federal government and “Operating and facilitating financial institutions” under the state government. As discussed earlier, this creates a confusion since the policy, law, criteria and regulation would determine the operation of banks in Nepal. One explanation could be through the German model which concentrates legislature at the national level and executive function at the provincial level. But, the same is not explained anywhere. Even if such is the case, it is very easy for blame game to occur between state and federal governments. This presents us with the first problem as the constitution does not define the nature of conflict. Most likely the conflict will be pushed to the Constitutional Bench as directed under Article 137.

As per the constitution, it clearly states that majority of the macro-economic policy powers of the sector rests within the federal domain, though states are allowed to control operations of these institutions. The same is designated in accordance with Nepal Rashtra Bank Act, 2002. Operational activities could include regulation of digital banking facilities, branching strategies or product innovations. Since NRB Act controls licenses to commercial banks and financial institutions and regulates, inspects, supervises and monitors such transactions, the scope of differentiation that could be achieved with the power is limited. It may provide the opportunity for states to create their own respective public banks which may cause further deliberation. A state bank may use protectionist policies which will directly come in contradiction with constitutions’ spirit. The main issue regarding this arbitrary allocation is no added benefit with this distinction. On the contrary, it may lead to opening a Pandora’s box of problems thus adding to the workload of the constitutional bench. Moreover, federalism by nature gives rise to healthy competition of goods and services within jurisdictions. Banking and Financial Institutions further exist to aid such competition thrive rather than engaging in such competition themselves. This kind of competition is often seen to create a bubble with chances of causing disruptions in the economy.

The unbundling report does make a distinction between financial institutions which are not regulated under the central bank or cooperatives which may act as small time financial institutions. Cooperatives would be governed under states and they are free to choose the policy and coordination of these institutions. However, a rigid framework legislation for the regulation of cooperatives is required for these to function.

Additional challenges that need to be answered under this segment include: lack of human resource capacity for states to adequately meet the demands of its citizens since about 400 local level governments lack proper banking facilities. The operation is under states but with the lack of capacity, is the central government then empowered to intervene and create a standard procedure to solve this problem?

Within the sample of the federal countries studied, a majority put banking and financial institutions under the federal government. The prime reason is to maintain uniformity and ease of maintaining national accounts; more so in an under-developed economy. United States of America, by contrast, has a dual banking system. Though not similar to the Nepalese variant, the dual banking system allows states and national bodies to charter and supervise BFIs at different jurisdictional levels. Following erratic fluctuations in the economy in the last century, the federal government has assumed a greater role of late. Hence, it should be worth considering to revise the reasons the lawmakers had in mind to distinguish the role as per the current constitution.

Table 6: Detailed Functional Analysis on BFIs⁶²

S.No.	Major Function as (policy instrument)		Sub-functions	Role of Government at Various Level of Services			
				Regulations/Standards	Financing	Provision	Production
Schedule-5							
1	Central planning, central bank, finance policies, monetary and banking, monetary policies, foreign grants, aid and loans	5.2	Economic, bank, financial sector and foreign grant assistance and debt				
		5.2.4	Policy, Law, Criteria, Coordination and Regulation related to banks and financial institutions	F			
		5.3	Central Bank, Financial Policy, Currency and Banking and Monetary Policy				

62 For all functional analysis; F refers to Federal Power, S refers to State Power and L refers to powers executed and legislated by Local bodies.

		5.3.6	Inspection and regulation of payment system and clearance house and relief	F			
		5.3.7	Contact and coordinate with banks and financial institutions	F			
		5.3.12	Establishment, supervision and regulation of commerce banks, development banks and financial institutions			F	
2	Insurance policies, securities, cooperatives regulation	28.1	Insurance policies, securities				
		28.1.1	Insurance policy, laws, criteria, and regulation	F			
		28.2	Cooperatives regulation				
		28.2.1	National policy, laws, criteria and regulation related to cooperative	F			
		28.2.2	Permission and regulation of Cooperative Bank, which will be established at national level	F	F	F	F
		28.2.6	Inter-state cooperative coordination	F			
		28.2.8	Promotion and operation of cooperative sector	F		F	

Schedule-6							
3	Operation of banks and financial institutions in accordance with the policies of Nepal Rastra Bank, cooperative institutions, foreign grants and assistance with the consent of the Centre	2.3	Financial Sector				
		2.3.1	Operating and facilitating financial institutions			S	
		2.3.4	Co-financing as per federal policy		S		
		2.4	Cooperative organization				
		2.4.1	Regional policy, laws, criteria, implementation and regulation related to cooperative organization	S			
		2.4.2	State level cooperative, cooperative association, cooperative bank related permission, operation and regulation	S		S	S

Source: Constitution of Nepal, Cabinet Unbundling Report, 2017

LABOUR MARKET

Laws concerning the labour market, be it general laws, trade unions or skill development are a greater concern in the Nepali context. Since time immemorial, it is a well understood fact that Nepal's most prosperous export has been its labour in the international market, be it in terms of armed forces or industrial workers. Having said that, it lacks standards for most other professional skills due to a lack of directed government policy. The discourse is one of crucial importance as Nepal also enjoys a young population dividend, which if carefully harnessed could turn into an asset for the country. Refraining from the debate on Nepali labour exports, it is important to shift focus on the agenda of how human resource development could be utilised as a major contributor to the economy. As pointed out in our consultation meetings, Dhading has no labour for the reconstruction after the earthquake; while Nepalis are moving abroad to build other countries, Nepal itself does have any labour to build itself. A major portion of the Nepali workers operate in the informal sector. The broad base policy under the unitary system did not produce an investment-conducive labour policy resulting in countless strikes and bandhs for several decades. Even though these have drastically reduced in recent times, the labour laws are still archaic. The state governments need to come up with their own set of labour laws to foster a speedy development which would also enhance the business climate in the country.

SKILL DEVELOPMENT

Skill development, along with education has become increasingly focused agenda of the governments especially among OECD countries to ameliorate the quality of their human capitals. In Switzerland, vocational education and training or VET system has been quite effective in producing competent human resources. This program is jointly regulated by the confederation and cantons. On the other hand, Canada delegates the regulatory authority over apprenticeships to provinces and territories. With different federal countries

within the OECD circle dividing the power with respect to skill development in contrasting manner, it is difficult to pinpoint an ideal scenario for Nepal. Nepal, contrary to most nations, has designated pockets of localised skills which further aid trade and commerce to enhance quality. The same is reasoned due to a variation in geography and local industry. While the mountain abundant states would effectively contribute to providing trainings for climbers, the mid hills would shift focus to hospitality; for example. Thus, a unilateral policy would prove to be ineffective in the Nepali context. Skilled labour would produce a desired quality of international competitiveness turning a defunct industry into a profitable venture.

Skill development in Nepal, just like in Switzerland, comes under the joint jurisdiction of federal and state governments as mandated by the constitution of 2015. A factor to be minutely understood in the given context is the variation in skills required in the country's development. Furthermore, the political reality of the country has not favoured a collaborative feature. Rather than forcing collaboration, individual sub-national units could be incentivised to harness their own development programs free from the intervention of the national government. We can use this function as a testing ground and confer exclusive power on the state level to verify how well the lower tiers of government are actually able to utilise the autonomy they have been given. The same stems from another reason which would empower the state to focus on this pressing need while the federal could be mandated with national priorities. This could in turn provide a sense of independence to the states and municipalities as well as offer assurance that they are an integral part of the federalism. Credibility of regional government could also strengthen in the eyes of the citizens when they (state and local levels) have the sole authority to command over certain functions. Since these institutions are essentially the representatives of the local people in a federal structure, it is crucial for them to gain trust of the locals and prove accountability.

Whether the state and local governments entirely taking control over regulatory matters of skill development would prove efficacious or not is unclear. However, what this course of action generates is the empirical evidence on the extent of compatibility of regional governments.

LABOUR LAWS AND TRADE UNIONS

Nepal ranks among the top countries for man-days lost. It not only affects the economic health of the country but also does not improve working conditions. Labour laws time and again have been a major factor in worsening employer-employee relations. The diversity of differentiation in the labour market of Nepal should be a major argument against a federal intervention. Laws establishing safety concerns, rights of labour and compensation will vary given the type of economic activity they are engaged in. Furthermore, the true realisation of the federal principle could only be achieved by empowering the sub-national units to enact policies that they seem fit for their jurisdictions.

Given the political reality of the Nepalese landscape, labour laws and trade unions should be restricted to the states, which gives them the opportunity to develop their own mechanisms of resolving disputes and establishing a strong employer-employee relationship, a feat unheard of in Nepal. Within the sample, the said power is jointly administered by the federal and the state level government but a word of caution to be noted in the matter is when the two arrive at a conflicting situation, the federal always wins given its constitutional status. This is not the case in Switzerland and USA where the sub-national units are empowered to follow their own practices free from the intervention of the central government. Labour Laws have also been seen as an obstacle to transparent government as it significantly encourages the rise of mafia concentrations. A strong argument in favour of the states is the benefit of learning from others. In our consultation meetings, it was even suggested that local governments should also be empowered to draft labour laws. This view was raised given labour requirements would vary greatly from municipality to municipality.

The issue of cross border labour laws was also raised by experts during the consultation meetings – Nepal currently does not have a robust and comprehensive mechanism to employ foreign labourers in the country. Hence, a detailed study and legislation is required to manage foreign

labourers coming in Nepal. Since all international matters are under the purview of the federal government, the states do not have the authority under the constitution to make laws under this section. It should also be noted that the role of the central government should not override the state governments' efforts. Hence, a strong, independent, impartial umpire in the form of the constitutional bench is the need of the hour.

Table 7: Detailed Functional Analysis of Labour Market

S.No.	Major Function as (policy instrument)		Sub-functions	Role of Government at Various Level of Services			
				Regulations/ Standards	Financing	Provision	Production
Schedule-7							
11	Social security and employment, trade unions, settlement of industrial disputes, labour rights and disputes related matters	11.2	Employment, trade union, settlement of industrial disputes, labour rights, dispute related matter	FS	FS	FS	
		11.2.4	Policy, law and regulation regarding trade unions	FS	FS	FS	
		11.2.5	Labour force, labour market study, research and labour force plan	FS	FS	FS	

		11.2.6	Industrial dispute resolution, labour relations and judicial disclosure	FS	FS	FS	
		11.2.7	Workplace Safety, Factory Inspection and Regulation	FS	FS	FS	

Source: Constitution of Nepal, Cabinet Unbundling Report, 2017

BUSINESS CORPORATIONS

With the promulgation of the federal constitutions in 2015, a degree of decentralisation especially with respect to the different aspects of business entities was expected. These included business entity incorporation, access to credit, contracts and bankruptcy. However, the same did not reflect in the latest Industrial Enterprise Act, 2016. While the same may be devised on the need of the hour, its features do not reflect the division of powers, and gives responsibility to the centre to manage all affairs within the scope.

The subjects of incorporation, contracts, partnerships, bankruptcy and insolvency are given to the joint competence of federation and state. The same could not translate into a blessing due to the inherent control of the federal government over the laws that have already been passed. In turn, it means that the states could not make alterations to the laws primarily because if they go against the centre, the same would be defeated. This does not create the proverbial laboratory conditions which is a prime advantage of a federal setup which results into successful policy making. Moreover, the geographical terrain and lack of connectivity in the country makes it difficult for registrations to be concentrated in the states. Thus, local governments additionally need to be in charge of incorporation, registrations, permits and closure of business enterprises. Further, information dissemination should be the prerogative of the local governments since they are the closest to the citizens.

Incorporation of enterprises is jointly regulated by the federation and states. A major problem arising from the same is attributed to duplication of policies thus leading to confusion and conflict. Additionally, in terms of capacity, the states would need the requisite institutions to be able to make the process easier for companies to register and operate their businesses under the law. Access to these institutions in terms of time, distance and policy is a challenge that needs immediate attention. It is also pointed that the regulatory bodies in Nepal are weak. Thus, regulatory bodies need to be strengthened for easy access and oversight ensuring a rule of law in the country which in turn fosters a healthy business climate in the country.

A major problem faced by businesses is the existence of syndicates and associations that form cartels and hence deter the growth of additional businesses. A major example is the transportation sector which faces a lack of innovation due to strong cartels everywhere in the country. Thus, state level differentiation in laws may help break these cartels and improve a competitive environment.

Dispute resolution is another area in which Nepal performs poorly. The creation of specialised courts comes under the jurisdiction of the federal government⁶³; state high courts do not have the power to create tribunals or establish commercial divisions to aid in dispute resolution. Thus, the process is largely concentrated in federal hands which may delay the formation and speedy resolution of disputes.

While the given spectrum gives a majority delegation to the federation and state, caution must be utilised to study it in Nepal's point of view. The Industrial Enterprise Act sheds some light on the different categorisations that industries are segregated on; micro, cottage, small, medium and large based on the size. For cottage industries (even though listed under the same subsection) a different feature list is provided in the annexure of the bill which forms the classification criteria. The industries are also divided on the nature of the goods and services produced; energy, manufacturing, agro-based,

⁶³ specialized courts can only be created by the federal government under the Supreme Court

minerals, construction, tourism, information and broadcasting and services. It should be noted that all the rules, regulations and laws pertaining to these sectors are currently governed under the federal regulations. There should be a considerable effort to encourage states and local administration to form their own rules and regulations pertaining to their needs and requirements.

The Constitution of Nepal aptly does not distinguish the division of power relating to the different aspects of business corporations as detailed in the Industrial Enterprise Act. It should also reflect in the division of powers between the three jurisdictions guided by the principles of subsidiarity, externalities and spill-overs. The micro category could be allocated to the local level, cottage, small and medium to the states while the federal could look at large corporations which tend to have a nation-wide spread.

A case for equal treatment of government and private businesses is also required in the country. The constitution creates an equal status for all citizens which is inclusive of the government as well. Thus, it should be noted that government businesses should not be given preferential rights or treatment and should be governed under the same laws as other Nepali businesses operating in the country.

Table 8: Detailed Functional Analysis on Business Corporations

S. No.	Major Function as (policy instrument)		Sub-functions	Role of Government at Various Level of Services			
				Regulations/ Standards	Financing	Provision	Production
Schedule-5							
18	International trade, exchange, port, quarantine	18.1	Policy, Law, Criteria, Planning, Implementation, and Regulation of International Trade	F	F	F	

		18.4	Relationship, Agreement, Agreement, Implementation and Regulation with the International Union of International Trade and Transit	F		F	
		18.5	Multiple shipping policy, laws, criteria, plans, implementation and regulation	F		F	
		18.6	Interim trade policy, laws, simulation and regulation	F		F	
		18.7	Construction and operation of cargo warehouse, dry harbor, container freight station, clearing / forwarding and undertaking service	F	F	F	F
		18.8	National criteria and regulation of business-related firms and institutions	F			
		18.9	Development, expansion and operation of the physical infrastructure of international trade	F	F	F	F

		18.10	Operation and management of integrated checkpoint at the international border point	F	F	F	F
24	Intellectual property (including patents, designs, trademarks and copyrights)	24.1.1	Policy, Law, Criteria, Implementation and Regulation regarding intellectual property including patent, design, trademark and copyright	F	F	F	F
		24.1.2	Management and promotion of intellectual property including patent, design, trademark and copyright	F	F	F	F
		24.1.3	Contact, cooperate and coordinate with the International Association of Intellectual Property including patent, design, trademark and copyright	F	F	F	F
28	Land use policies	29.1.1	Land use policy, law, criteria, planning and regulation	F			

		29.1.2	The use of land, capability and relevance of land	F			
Schedule-6							
11	Intra-state trade	11.1.1	Trade / commercial policy policy, laws, criteria, plans, implementation and regulation	S			
		11.1.2	Regional trade promotion, simulation and regulation			S	
		11.1.3	Building, operating, collaborating, facilitating, coordinating and regulating business infrastructure inside the state	S	S	S	S
		11.1.4	Transportation / transportation and cargo management	S		S	
		11.1.5	Trade-related Syndicate Cartling Control and Competitive Policy and Law, Criteria, Implementation and Regulation	S			
		11.1.6	Goods, services and intellectual property relations	S	S	S	S

		11.1.7	Registration, dismissal and regulation of business firms	S			
		11.1.9	Coordination and collaboration with private and non-governmental sectors	S	S	S	S
20	Factories, industrialization, trade, business, transportation	20.2.1	Factories and industrialization related policies, laws, criteria, plans, implementation and regulation	S		S	
		20.2.2	Industrial Business Promotion and Regulation	S		S	
		20.2.3	Industry, Permission, Renewal, Dismissal and Regulation	S		S	
		20.2.4	Establishment and extension of the industrial sector and the state's special economic zone	S	S	S	S
		20.2.8	Development of the state's public institution, industrial development and promotion, and regulation	S	S	S	S

Schedule-7							
2	Supply, distribution, price control, quality and monitoring of essential goods and services	2.1.1	Consumer Rights rights protection and promotion, Consumer consciousness awareness programs, implementation and monitoring	FS	FS	FS	FS
6	Acquisition, requisitioning of property and creation of right in property	6.1	Policy, Law, Criteria Creation, and Regulation of Property Acquisition, Acquisition and Creating Rights	FS		FS	
8	Matters relation to bankruptcy and insolvency		Law, Criteria, Implementation and Regulation of management of industries and business firms that are insolvent	FS	FS	FS	FS
21	Industrialization	21.5	Export of Industrial Goods	FS	FS	FS	FS
Schedule 8							
10	Local Market Management	10.1.1	Policy, Law, Criteria, Implementation and Regulation related to local business / commerce, demand / supply, market management and monitoring and consumer rights and interest	L			

		10.1.3	Production of local goods, import and export projection, pricing and monitoring	L		L	L
		10.1.4	Local Business / Commerce Related Infrastructure	L	L	L	L
		10.1.5	Monitoring and regulation of the value and quality of local goods and service trades	L	L	L	L
		10.1.6	Local-level business firm registration, permission, renewal, dismissal and regulation	L	L	L	L
		10.1.7	Local business statistics system and study research	L	L	L	L
		10.1.8	Coordination and collaboration with private and non-governmental sectors	L	L	L	L
		10.1.9	Local business promotion, simulation and regulation	L	L	L	L
		10.1.10	Conservation, promotion and archiving of local intellectual property	L	L	L	L

		10.1.11	Consumer awareness enhancement, target management of target users and quality checking of local goods and services	L	L	L	L
14	Distribution of house and land ownership certificates	14.1	According to the state criteria, management of House and Land Ownership Certificates distribution system	L	L	L	
		14.5	Land dispute solution			L	

Source: Constitution of Nepal, Cabinet Unbundling Report, 2017

AGRICULTURE

Agriculture, in Nepal, accounts for about one third of its GDP while employing about two thirds of the country's population. With vast and diverse agro-ecological landscape of the terrain, Nepal can produce a large variety food grains and cash crops. While studying the cross section of devolved power in the agro-based industries, the broad term of Agriculture is a shared competence within all the three jurisdictions. Several other subjects which directly affect the sector fall within the purview of concurrency of Federation and State (Drugs and Pesticides, Supply, distribution, price control, quality and monitoring of essential goods and services, utilization of forests, mountains etc.), exclusively with the State (Agriculture and livestock development, use of forests), exclusively with the central government with relation to land use, and exclusively with the local in relation to operation and control of agricultural extension.

While segregating the concerned subjects, ambiguity about the exact nature and scope of each of these is apparent. The grouping and definitions of the subjects are not discussed in detail and this hence creates further problems in deciding the policies that each of these jurisdictions will control. Furthermore, the process of inter-jurisdictional conflict is not enumerated which also adds up to a fine kettle of fish. Blame game due to the lack of political maturity and coherence is easily predicted given the state of affairs throughout the Nepalese political history.

In the sample analysed, Agriculture is largely held within the sub-national governments. India also allocated the power exclusively to the states given the wide variety of agricultural output produced in the country. Nepal should make maximum out of its geographical advantage and for this, states should be granted autonomy in making agriculture development policies. Local units tend to be smaller with potential spill over effects and externalities and the federation is too large a territory to accommodate the varied diversity that the sector encompasses.

Specific problems dealing with value chain industry in the agriculture sector is seen as the most pivotal problem affecting this sector. Agricultural produce has various associated industries attached to it depending on the stages that it goes through – farming, producing, processing, packaging, marketing and sales. Since these industries do not tend to be concentrated in the jurisdiction of a local government or even a state government, lags in coordination and differentiated policies may potentially hamper growth in the sector. Thus, the federal government's role in designing an umbrella Act may potentially provide a strategic framework to tackle this problem.

Another potential problem discussed pertains to the financing model that Nepal needs to decide for the promotion of its agricultural produce. The agriculture sector has historically seen massive subsidies given which have proved to hinder competition and thus efficiency in the market. Thus, a robust mechanism to mobilise resources is required to aid growth and development in the sector.

It is noted that 'livestock' comes solely under the charge of state and local governments; the role of the federal government in policies relating to livestock are null. This is both a boon and a bane; states and local governments with differentiated policies could help develop innovative models for the promotion of fisheries and meat industry. However, a lack of standardisation encompassing the whole country might not meet the international standards which will then fail to develop a potential advantage of exporting these commodities in the international market.

The Indian states offer the best examples wherein, states have used differentiated policies to boost agricultural inputs as per their comparative advantage. In India, the state of Punjab produces export quality wheat and rice grains via the green revolution that has significantly boosted its own GDP while also adding significant revenues from the export. Similarly, Maharashtra has a comparative advantage with mangoes, Kerala exports spices and coffee, Assam and West Bengal have comparative advantage in the production of tea, Uttar Pradesh in sugarcane, Gujarat in dairy products and Sikkim, the first organic state in India has significantly added to its coffers through the high income organic food industry.

Table 9: Detailed Functional Analysis on Agriculture

S. No.	Major Function as (policy instrument)		Sub-functions	Public Good Output	Role of Government at Various Level of Services			
					Regulations/ Standards	Financing	Provision	Production
Schedule-5								
20	Agriculture and livestock development	20.1.1	Regional policy, law, criteria, planning, implementation and regulation related to agriculture, animal development and food nutrition		FS			
		20.1.2	Control of agriculture and animal pesticide and epidemic		FS			
		20.1.3	Agricultural industrialization, development and promotion of livestock industry business		FS			

		20.1.5	Registration, permission, renewal, dismissal and regulation of the parasvet according to national policy and criteria				FS	
Schedule-8								
15	Agriculture and animal husbandry, agro-products management, animal health	15.1.1	Local Policy, Law, Criteria, Planning, Implementation and Regulation related to agriculture and animal husbandry, agricultural production management and animal health		L			
		15.1.2	Agricultural and livestock market information, market and hitbazar infrastructure, small irrigation, training, technology dissemination, technical support, agricultural materials supply and farmer capacity development, operation and regulation				L	

18	Management, operation and control of agricultural extension	18.1	Agricultural Broadcasting, Local Policy, Law, Criteria, Planning, Implementation and Regulation		L			
Schedule-9								
4	Agriculture	4.1	National policy related to agriculture, law and criteria and regulation		FSL			

Source: Constitution of Nepal, Cabinet Unbundling Report, 2017

TOURISM

The tourism sector recorded a rise of more than fifty percent amongst most developing sectors in the country. With a figure of 69% rise in revenues, the tourism sector in Nepal employs about 3.5% of the total workforce while accounting for a net revue in the country amounting for 4.3% of the national GDP. The figures and government data analysis from the Investment Board clearly tag Tourism as a cash cow given the plethora of diversified opportunities available in Nepal.

The sector itself spreads over a wide spectrum of diversified purposes. While the bulk of the tourists enter Nepal with a vacation motive, holidaying and trekking/mountaineering; pilgrimage, business and official also contribute a significant portion to the reasons. This opens renewed investment and employment opportunities. Besides the rich mountain landscape, Nepal also enjoys a preserved cultural history, forest reserves, adventure sports as well as pilgrimage sites for world's Hindus and Buddhists. The emergence of Nepal as a top provider of MICE (Meetings, Incentives, Conferences and Exhibitions) tourism due to the favourable temperatures round the year and

the rapid development of the hospitality industries also add to the greater value of the sector to Nepal.

Tourism sector is jointly regulated by Federation and the States. While most sample countries allocate it as Nepal does, the cause of worry is the other sectors which indirectly feed to the industry. For example, the Annapurna Conservation Area is pegged as one of the best trekking trail destinations in the world, currently regulated by the National Trust for Nature Conservation would come directly within the Federal government. All trekking activities, development of routes, maintenance as well as the diversification of tourism activities would then be the sole control of the Federal government. Similarly, the central government also would control the regulation of the sites of archaeological importance – thus in effect, most tourist spots around the country would be a piggy bank for the central government with no say of the sub-national governments in place. Furthermore, the exercise of connectivity i.e. roads and air travel also lie at the hands of the federal government. It should be noted that that laws previously enacted need to be revisited and be adapted to suit the new system, failing to do which would mean that the federal country would effectively be governed as a unitary country with no benefit to the additional jurisdictions created.

Major issues in the tourism industry surround the case of Inter-State tourism policies. This is specifically targeted towards trekking routes which spill over multiple jurisdictions, thus creating externalities. A differentiated policy and service delivery in the maintenance and fee collection of trekking routes in multiple states might hamper the industry. It would additionally create coordination and confusion between the different orders of governments which might slow the pace of innovation in this industry. Hence, a robust and pragmatic solution needs to be worked out to aid growth and development in the tourism sector. The same could be addressed through a framework legislation but states should be left to design their own respective tourism packages and policies which will fuel a healthy competitive environment and attract more tourists to increase revenue.

Tourism is a private sector dominated industry. Cartels and association deter business growth and thus policies that aid businesses should be adopted to encourage entrepreneurs in the sector. Similarly, formalisation of businesses is also the need of the hour. Again, states and local governments could use tax breaks and other formats to incentivise businesses to formalise and capitalise on developing the sector for higher rates of return.

The Indian example yet again provides for a concrete evidence whereby, individual states have promoted tourism to help boost their economies. Specifically, the backward north-east states of Meghalaya, Arunachal Pradesh and Assam have even collaborated with artists and the entertainment industry to host international level concerts which attract thousands of tourists and help them grow. While the central government actively promotes tourism through the Incredible India project, individual states have also come up with attractive packages in partnership with private tours and travel companies and airlines to operate in a collaborative format to increase revenues.

Table 10: Detailed Functional Analysis on Tourism

S. No.	Major Function as (policy instrument)		Sub-functions	Role of Government at Various Level of Services				Justification/ Comment
				Regulations/ Standards	Financing	Provision	Production	
Schedule-5								
29	Tourism policies and environment adaptation	29.3.1	National Policy, Law, Criteria, Planning, Implementation and Regulation regarding Tourism Development	F	F	F	F	

		29.3.2	Contact, collaborate and coordinate with the International Tourism Organization	F		F		
		29.3.3	National Policy, Law, Criteria, Planning, Implementation and Regulation regarding mountaineering, travel and trekking	F	F	F	F	
		29.3.4	Development and international promotion of touristic destinations including natural, religious, cultural, archaeological, adventure	F	F	F	F	
34	Sites of archaeological importance and ancient monuments	34.1	Policy, laws, criteria, plans, implementation and regulation of spaces of archaeological importance and ancient monuments,	F	F	F	F	

		34.2	Protect, charge, study, research, excavation, rebuild the places that are listed as historically, archeologically, religiously and culturally important at both national and international level	F	F	F	F	
		34.3	Protection of contractual document of agreement with foreign nations	F	F	F	F	
		34.4	Policy, Law, Criteria and Regulation of national museum	F	F	F	F	
		34.5	Establishment, operation and management of National Museum	F	F	F	F	
		34.6	National Policy, Law, Criteria, Study, Research, Coordination and Regulation of Culture, Religion, Civilization and Heritage	F	F	F	F	

		34.7	Policy, Law, Criteria, Planning, Regulation and Management of World Heritage Committee	F	F	F	F	
		34.8	Archeology, cultural heritage, religion and traditions, contacts, cooperation and coordination with the international community	F	F	F	F	
Schedule-7								
18	Tourism	18.1.1	Policy, Law, Criteria, Planning, Implementation and Regulation of Tourism Development	FS		FS		
		18.1.2	Travel and registration agency registration permission and renewal	FS		FS		
		18.1.3	Promoting regional tourism	FS	S	FS	S	
		18.1.4	Development of regional tourism infrastructure	FS	S	FS	S	

		18.1.5	Tourist Police Management	FS	S	FS	S	
		18.1.6	Promotion, Registration, Permission, Renovation and Regulation of Tourist Hotels, Resort, Lodge, Travel Guide, Range etc.	FS	S	FS	S	
Schedule-9								
	Archaeology, ancient monuments and museums	12	Cultural area	FSL	FSL	FSL	FSL	
		12.1	Included in 18 of schedule 6					

Source: Constitution of Nepal, Cabinet Unbundling Report, 2017

POLICY INNOVATIONS THROUGH LABORATORY FEDERALISM

One of the finest virtues of federalism is attributed to its achievements in creating successful policy innovations in various sectors that help maximise the comparative advantage that each of the sub-national jurisdictions offer. Amongst these specific examples from United States of America, Australia and India have lessons for Nepal.

Australia's Digital Revolution⁶⁴

In Australia, many states looked to leading customer service delivery agency Service NSW as a model to beat or to copy, at the very least, because of its success in shifting the state's service transactions online, which is expected to be 70 percent digital by 2019.

The state of Victoria, whose online transactions currently sit at 1 percent, geared up to improve the number of government transactions that could be completed online. Victoria government's chief customer officer stated that their slow start gave them the opportunity to leapfrog digital government progress made by their counterparts in NSW, Queensland and Tasmania. A similar approach was embraced by Western Australia where the government handpicked a number of successful projects from other jurisdictions rather than reinvent the wheel.

Likewise, NSW signaled its intention to tap into the whole-of-government GovPass digital identity platform so that the NSW citizens could access both federal and state services through Service NSW. The state is also trying to be the first state to introduce digital drivers' license.

This competition between state and territory governments has driven

⁶⁴ <https://www.itnews.com.au/news/is-competitive-federalism-driving-australias-digital-govt-revolution-471023>

improvements in the service delivery sector and has helped achieve the digital strategy's goal of creating a 'data-informed and agile public service'. This competitive federalism has also increased replication and adaptation of successful practices, thereby increasing efficiency.

California paves way for beneficial federalism⁶⁵

The California Energy Commission is yet another example of federalism at its best through the setting of energy efficient standards. California has asserted leadership in setting appliance standards by investigating the mechanisms and policies that tackle inefficient appliances that further inflate the consumer utility bills.

California's long history of implementation of energy efficient standards has encouraged innovation and created a level playing field in the nation's biggest state-wide market. As a result of the efficiency standards introduced by California, the new refrigerators use 75 percent less electricity and cost half as much. Similarly, washing machines use 75 percent less energy while dishwashers draw half as much power. These standards have not only helped the consumers save over a trillion dollars, but also helped businesses thrive.

Likewise, in 2016, California successfully adopted first-in-the-nation energy efficiency standards for computers and monitors with the support of the industry, consumer and environmentalist advocates. These standards, if properly instigated, would save enough energy to power 350,000 California homes per year. The state government also aimed to expand to a number of important areas including 'energy vampires'. The energy vampires are appliances or devices with an 'always on' mode and continue to pull electricity while not in use. A study showed that 23 percent of the electricity consumed in California was flowing to devices that were either switched off or in standby mode. Even though it is a complicated problem to solve, California has taken the right approach on this issue.

Since the Great Recession, California's per capita income has grown 1.6

⁶⁵ <http://thehill.com/blogs/pundits-blog/energy-environment/342973-california-sets-the-gold-standard-on-good-energy-policy>

times faster than that of the rest of the U.S. State leaders from around the U.S. could look to California to for a business-friendly path to develop standards that would prevent discord and encourage cooperation.

California's effort to push energy efficiency policy forward exhibits an example of self-sufficiency and dedication that can be replicated nationwide.

Competitive Federalism in India to attract foreign investment⁶⁶

Telangana, India's youngest state stood at the forefront with a 10.1 percent growth rate in 2017 as compared to an undivided Andhra Pradesh (AP) with a 2.7 percent growth rate in 2012-2013. This double-digit growth rate was achieved under the stewardship of Kalvakuntla Chandrashekhar Rao. Among the states that received industrial investment in 2017, Telangana stood 3rd. The introduction of government's new industrial policy, namely, Telangana State Industrial Project Approval and Self-Certification System (TS-iPASS) significantly contributed to this investment surge. This policy introduction attracted a cumulative worth of \$11.2 billion and helped create 240,000 jobs in the state.

The state also topped investment growth, with an aggregate of 79 percent, among its southern peers. Telangana's chief minister set attracting investments as priority and for that he not only relaxed power relations, but also aimed at setting up offices in various countries to promote state policies and institutions. This considerable effort shown by the Telangana government managed to draw international giants like Uber, IKEA and DreamWorks, along with Google, Amazon and Apple. Additionally, the Telangana government signed a pair of Memorandum of Understanding (MoUs) with Sany Group, a Chinese construction equipment company to set up a prefab factory in the state.

Andhra Pradesh, under the leadership of Chandrababu Naidu, did not

⁶⁶ <https://thediplomat.com/2017/10/competitive-federalism-in-southern-india-a-case-study-of-andhra-pradesh-and-telangana/>

fall behind either. Compared to Telangana's 79 percent, AP successfully achieved a 50.8 percent growth. The government also signed an MoU with the Performance Management and Delivery Unit (PEMANDU) under the Malaysian Prime Minister's Office that will assist AP in attaining growth and development. Likewise, another MoU with Singapore-based Ascendas-Singbridge Pvt. Ltd. and Sembcorp Development Ltd. to develop Amaravathi was signed by the AP government.

When Telangana came up with TS-iPASS and T-HUB, AP came up with the First IT and single desk clearance policies. Both AP and Telangana are competing in their efforts to digitize, encouraging digital transactions and setting up e-purses. This clearly indicates that both states are engaging in competitive federalism, something that has been widely encouraged.

AREAS FOR REFORM

The Constitution of Nepal through Part 31 provides for the method and procedure to make such reform. The active role envisioned for the State assemblies provides for a robust system with an inclusive principle. It should be noted that the local bodies do not play any active role concerning the amendment procedure. Based on the study conducted in relation to division of powers, the following recommendations should be discoursed on:

RESTRUCTURING OF LEGISLATIVE LISTS i.e. SCHEDULES 5, 6, 7, 8 and 9

The above-mentioned schedules enumerate the powers that each of the jurisdictional governments are responsible for – 5, 6 and 8 are exclusive jurisdictional competencies for federal, state and local levels respectively while 7 and 9 are concurrent powers between federation-state and federation-state-local levels. These lists though coherent in structure with the clauses of the constitution are not coherent in the manner of delegating responsibility. There are two broad categories under which reform could be initiated:

Grouping of Subjects: The list of competencies is grouped without a common denominator thus making the list haphazard with a list of possible interpretation flaws. Examples of such groupings include:

Schedule 9 – S.N. 2: Education, health and newspapers

Schedule 7 – S.N. 18: Tourism, water supply and sanitation

Schedule 8 – S.N. 10: Local market management, environment protection and bio-diversity

Subjects in Multiple Schedules: The 5 schedules total to 108 points, a portion of which appear in multiple lists with no explanation on the scope and nature of the competence. This not only creates confusion with respect to which

jurisdiction is responsible for which subject but also creates overlapping allocation of resources by multiple jurisdictions. Examples of such include;

- Health features in almost all schedules with no distinction of the nature and scope of responsibilities that each jurisdiction needs to cater to.
- Statistics are maintained at each jurisdictional level. These statistics feed not only national accounting but also help businesses prepare future proposals for expanding markets in Nepal.

Subject Definition: The subjects are written as words with no explanation regarding the scope of the power each jurisdiction is allowed to use. Although the exercise has been initiated by the Local Governance Bill 2017, a state and federal version of the same is expected in a few months. One of the first exercises would be to develop a well-defined nature of responsibilities that each government is responsible for. This not only helps the governments to understand their work but also helps the citizens make informed choices with respect to the elected governments on various levels they choose.

Reassignment of Functions: The discussion put forward through the sectoral and regulatory review in the previous section points to a possibility in restructuring of legislative lists. Although this is not an urgent issue that needs to be on number one priority, it does add to constantly update the constitution and by extension the reassignment of functions in the legislative lists for improved implementation of the federal process.

COOPERATIVE GOVERNMENT

The constitutional nature of the government is defined to be of the cooperative nature. Emphasized by Article 232 of Part 20, Interrelations between federal, state and local governments; this cooperation is translated in various forms in the government. Schedules 7 and 9 are shared competencies which allow law to be multi-fold in terms of legislation and execution. Similarly, Direct Coordination Committees (Article 220) and Inter-State Councils

(Article 234) are bodies which foster interaction between the different jurisdictional governments to come together and resolve disputes. But all over the constitution the supremacy and over-riding powers of the Federal government tend to a centralised structure that the country previously also maintained. Nepali politics is a visible compromise since the inception of the first constituent assembly. The contemporary changes even today reflect the political bargain that plays out in the background. This puts a question on the stability of the political environment and implementation of the federal project in Nepal.

Thus, instead of the federal government being given over-riding powers, the Inter-State Council and DCC's should be empowered to solve disputes. Not only does it bring all stakeholders on the same table but it also unloads a possible mafia culture that may develop. Multiple international examples have been discussed in terms of regional governments being treated unfairly and the citizens moving towards secessionist movements as in the case of Catalonia in Spain and Quebec in Canada. The cooperative government should ensure to treat all levels with an equal status rather than being subordinate to the over-arching central government. The federal idea stems from the same problem and it is a must that the constitution should address.

EXCLUSIVE VS. SHARED POWERS

Concurrency or joint competencies also guarantees cooperation in some measure as it allows multiple jurisdictions to cater to spill over effects of a legislation. However, in the case of Nepal where the central government is already very strong, the state and local governments will have to fight for change every time. Thus, lists should be drafted to allow more powers to the states and local units. This in turn means to reduce the burden of the central government and to make state governments accountable to their people. Water-tight lists like the Canadian federal model is a prime example of the best practice amongst the countries, not only making state and local governments more efficient, the various issues would be dealt directly by the

governments closest to the people. It would also induce a competitive nature to encourage sub-national governments to improve service delivery and adapt best practices from the diverse pool available. This is also conducive to economic growth as varied practices will inform the different methods of innovating routes to prosperity. Thus, the constitution should adapt a water-tight model and when the time comes for a national consensus on a particular matter, the states as enumerated by Article 232 would request the federal government to initiate action. Subjects and Sectors should be allocated to the state governments with service delivery to the local levels.

FRAMEWORK LEGISLATION

Most legislation enacted before and after the promulgation of the Constitution have bestowed powers to federal government agencies for the enforcement and regulation. As per the new constitution, many critical tasks of development, regulation and business facilitation have been assigned to subnational governments. A mammoth task at hand is then to reformulate all legislation to fully make them compatible with the spirit of new constitution. The German experience renders a unique feat that could help solve the particular problem. In Germany, the central government is responsible for legislating all subjects while the regional governments are in charge of execution.

This model, though efficient, has its own flaws; ‘joint-decision’ trap is one being increasingly discussed in discourse. But it does provide for the problem that Nepal faces. Rather than repealing all previous legislation which not only consumes effort and endless debate but also time, the framework legislation model could be adapted here for the Nepalese context to convert all existing legislation in terms of rules and regulations so that the states could adopt the same with the execution model they would want to further depending on their requisite needs and requirements. Framework legislations are also part of the Brazilian and Mexican constitutions. This is especially important for progressing the agenda of economic growth since major laws – Company

Act, Industrial Enterprises Act etc. directly affect the business environment in the country.

COMMERCIAL CODE

The Constitution of Nepal does not have a section devoted to the commercial code even though article 236 gives explicit direction to prohibit anti-competitive policies (including taxation) to carriage of goods or extension of services within the country. It also does not make any reference to the production of such goods and services. The main legislation close to a commercial code would be the Industrial Enterprise Act, the Companies Act and to a large extent the Banking and Financial Institutions Act.

However, the same are a product of yesteryears with no relevance to the governance structure envisioned by the new constitution. Thus, it would be a relevant exercise to develop a single commercial code, a framework legislation detailing a new revised intent of multiple governments with responsibilities so as to benefit the people. Many countries, irrespective of a federal status have a commercial code which uniformly applies to all countries. With the explicit benefit of streamlining the routes to progressive economic growth in a country, a commercial code also protects citizens against political instability and pressures on political fronts.

CONCLUSION

Woodrow Wilson, the 28th President of the United States of America, in his seminal work, *Constitutional Government in the United States* 1908, famously redefines constitutions as a living being. A reflection of society of the present times granted to the citizenry as a right to free society from the predecessors.

“Society is a living organism and must obey the laws of life, not of mechanics; it must develop. All that progressives ask or desire is permission - in an era when “development,” “evolution,” is the scientific word - to interpret the Constitution according to the Darwinian principle; all they ask is recognition of the fact that a nation is a living thing and not a machine.”

The same is understood as a fact given multiple countries adopt the living constitution parable – the Canadian Federalism elaborates it in their living tree doctrine whereby, a constitution is organic and must be read in a broad and progressive manner so as to adapt it to the changing times while the first Indian Prime Minister noted a similar doctrine in his constituent assembly speeches;

“Vast number of minds and eyes look in this direction. We have to remember them. Hundreds of millions of our own people look to us and hundreds of millions of others also look to us; and remember this, that while we want this Constitution to be as solid and as permanent a structure as we can make it, nevertheless there is no permanence in Constitutions. There should be a certain flexibility. If you make anything rigid and permanent, you stop a Nation’s growth, the growth of a living vital organic people.”

The remaking of Nepal into a functioning federal country that meets diverse sets of needs will be evidence to its citizens that democracy was worth fighting for because it delivers. Thus, Nepal too, in the spirit of evolving future identifies and potential prosperity, should adopt the principle of the Constitution as being a living, both agile and adaptable, document.

CONSULTATION EXPERTS

S. N	Experts	Position/Organization
1	Mr. Ajay Pradhananga	Managing Director, Fleur Himalaya
2	Mr. Amar Raj Bhattarai	Confederation of Nepalese Industries
3	Mr. Ashok Silwal	Press Advisor, Nepal Tourism Entrepreneurs' Association
4	Mr. Bashu Aryal	Country Program Officer, IFAD
5	Mr. Bhanu Dabadi	Director of Strategy, National Banking Institute
6	Ms. Bimala Kesari Amatya	Lalitpur Municipality (Patan Durbar Square)
7	Mr. Bishnu Prasad Gyawali	Director, Department of Cottage and Small Industry
8	Mr. Bishmaraj Angdambe	Former Chairperson, PCIC & CW
9	Mr. Chudamani Bhattarai	Executive Director, FNCSI
10	Ms. Darshana Shrestha	General Secretary, FWEAN
11	Mr. Dev Bhakta Shakya	
12	Mr. Dhan B. Thapa	Head of Programs, National Banking Institute
13	Ms. Geeta Kumari Humagain	Registrar, Office of Company Registrar
14	Mr. Kamal Prasad Pageni	Parliamentarian (Member - Nepali Congress)
15	Ms. Kopila Dangol	Program Manager
16	Mr. Lal Babu Yadav	Parliamentarian (member of CPN-UML)
17	Mr. Mani Raj Lamichhane	Officiating Director, Nepal Tourism Board
18	Mr. Matrika Niroula	Lawyer/ ADR Practitioner
19	Mr. Pavitra Bajracharya	Chairman, Nepal Retailers' Association
20	Mr. Prachanda Man Shrestha	Former CEO, Tourism Board of Nepal

21	Mr. Pramod Nepal	Under Secretary, Ministry of Tourism
22	Mr. Pranil Kumar Upadhyaya	Advisor, Nepal Tourism Board
23	Mr. Pushpa Raj Acharya	President, The Himalayan Times
24	Mr. Radheshyam Adhikari	Planning Advisory Committee, KUSL
25	Mr. Shankar Aryal	Director General, Department of Industry
26	Mr. Shyam Prasad Giri	President, FNCSI
27	Mr. Subash Niroula	Executive Head, Nepal Tourism Board
28	Ms. Sunita Nemaphuki	Chairperson, R&D Innovative Solutions
29	Mr. Salik Ram Poudel	Agriculture Extension Office, Department of Agriculture
30	Mr. Kul Prasad Pandey	
31	Hon. Dr. Yubraj Khatriwada	Minister of Finance, Government of Nepal
32	Mr. Rameshore Khanal	Ex-Secretary, Ministry of Finance

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ANNEXURES

Annexure 1 : Economic Indicators from 1990-2017

Indicators/	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Date																												
GDP (current US\$) in Billion	3.2	3.9	3.4	3.6	4.6	4.4	4.5	4.9	4.6	5.3	5.4	6.00	6.05	6.3	7.2	8.13	9.14	10.3	12.5	12.8	16.0	18.9	18.8	19.2	20.0	21.4	21.1	
GNI per capita (US\$)	210	210	200	190	200	210	210	220	210	220	230	240	240	260	280	310	340	370	440	480	540	600	690	720	730	740	730	
Population below poverty line																												
Net Income	108.2																											
Personal Remittances Received (% of GDP)	111.2	128.9	152.4	151.9	230.1	263.6	245.5	301.9	333.1	340.3	390.3	954.4	1,058	1,178	1,538	1,78	2,088	3,248	3,428	4,088	4.78	5.38	6.28	6.58	7.58	7.48		
Foreign Aid (Grants % of revenue)	31.49	34.82	32.37	35.39	27.42	27.17	30.93	30.63	29.32	26.22	27.95	26.52	28.41	34.49	32.21	34.38	31.71	30.39	29.49	26.11	26.11	28.33	25.72	21.66	22.78	20.90	19.65	

Annex 2:

Measure	Baseline - pre 1948	1948	1951	1959	1962	1967 Amendments	1990	2007 (interim)	2015
Extent of central authority	Rana Oligarchy	A46-47 - king can assume all powers in emergency; A34 - king can block consideration of any bill; A19 - scope of authority is subject to the center & higher-level region	Absolute	Absolute - see for example A63, A10, A42, A55	Absolute	As per 1962	Absolute	Absolute	A232 - Government may issue directives, President may dissolve institutions in some circumstances; A234 - Inter-Provincial Council for dispute resolution
Scope of unit's autonomy	n/a	A19 - Panchayats have education, welfare and the prosperity of the people and the territory under their charge, including justice, water supply, basic education - implementation only	A6: Majesty to take steps to establish Village Panchayats	No units	A30-32 - Establishment of Village, Local and Regional Panchayats, general purpose role only.	A18-19 Principles of Panchayat system added	A104 and 46(1) - mentions Local Authorities	A138/9 - provides for federal system and local governance	Part 5 and associated schedules set out division of powers for provincial and local levels
Constitutionalism	Nil	A67 - judicial committee of legislature to resolve disputes and interpret constitution (semi-independent); A68 - review to be held to consider changes (king to implement)	Interim Act only (see preamble); otherwise king decides interpretation, changes etc.	A53: two-thirds majority required; A54 - Supreme Court interprets (but A57 - appointed by king at his discretion)	A82 - king can unilaterally amend constitution; A71 - Supreme Court jurisdiction extends to fundamental rights only	No change	A116 - 2/3 majority required; A88(2) - Supreme Court has jurisdiction in relation to courts	A148 - amendment requires 2/3 majority; A1027 - Supreme Court has jurisdiction	A274 - 2/3 majority required for amendment; A295 - provision for a federal commission and provincial and other level amendments; A114 - jurisdiction of supreme court only re fundamental rights; A234 - interstate council for dispute resolution established but numbers weighted to center
Bicameralism	n/a	A22 / Sch A - 36 of seventy seats in upper chamber comprised on Panchayat representatives	A34 - Advisory Assembly to have members appointed by the king as representative of regions, classes and interests	n/a	A34 - National Panchayat includes representatives of Zonal Assembly (and some appointed members)	A33 - Zonal Assembly comprises representatives of the lower level Panchayats (added)	A46(1)(c) Local Authorities and regions represented in the upper house	n/a	A86 - 56 of 59 members of upper house provincial and local level representatives; A275 - consent of provinces to changes to provinces required

Legislative executive relations	unelected Rana oligarchy	A7 - executive a mix of representatives of Ranas, king and Panchayats (elected) - with at least two from elected legislature - but A6 - are subordinate to the king	A58(a) - Advisory Assembly may seek resignation of executive, but decision subject to king; A25-27 - executive appointed by and responsible to King in whom executive power is vested	A13 - PM appointed by king on account of having confidence of legislature, Ministers appointed on recommendation of PM	Part 7 - executive power vested in king	Part 7 (26) - Introduction of PM and Cabinet from national legislature, still responsible to the king (50% score)	A36 - PM (commanding majority) and Cabinet appointed from legislature	A38 - PM appointed on consensus of seven major parties and Maoists, or two third majority of PM commanding majority of house	A75-76 - Council of Ministers has executive power and appointed by PM commanding majority of house
Basis of units (identity / territory)	n/a	Panchayats incorporate identity where territorially clustered	A6: Majesty to take steps to establish Village Panchayats - accounts for identity where territorially clustered	n/a	Establishment of Village, Local and Regional Panchayat, general purpose role only - accounts for identity where territorially clustered	No change	A104 and 46(1) - Local Authorities incorporate identity where territorially clustered	Mixture of territorial and identity based criteria (see CDRSP 2010 for example)	Not yet delineated
Sub-units (autonomous zones)	n/a	n/a	n/a	n/a	S30-32 - Village/Municipalities (thousands), Local (75) and Regional (14) Panchayats, VDCs/Districts/Zones	n/a	n/a	A56 provision for autonomous regions to be created	n/a
Local government (no. of levels)	n/a	Three - A16-22 - state legislature; Zilla Panchayats; Gram and Nagar Panchayats	Two - center and local	One	As per 1962	Four levels of government (as per 1962), though none constitutionally empowered	(At least) three levels of government to be established (see above)	Three levels of government (centre, provinces and local level)	n/a
Degree of asymmetry	n/a	A16-22 - Village (Gram) Panchayats less autonomous than town (Nagar) Panchayat	n/a	n/a	n/a	n/a	n/a	n/a	n/a

		A16 - 5-15 members voted by adults with necessary qualifications (effectively multi-member districts), and section 2(2) Sch A which provides for mix of elected reps (being Panchayat reps), and appointed interests	S34 - Advisory Assembly General to have members appointed to by the King as representative of regions, classes and interests - for purpose of advising on new constitution	S24 - House of Reps electoral division delineation to take account of diversity of inhabitants (among other things), but FPTP - S19 - senate, half elected by the House of Reps according to a fully PR system, half appointed	No explicit means; FPTP in single-member constituencies (see Nohlen et al 2001)	A35 - National Panchayat - only people registered in government-sponsored class and professional organizations (for peasants, labourers, students, women, former military personnel & college graduates)	A46(1) - out of 60 member upper house, 35 are elected via proportional representation, 15 appointed by king on basis of expertise, and fifteen elected at the local level by local officials;	A45 - Legislature/Constitutional Assembly to include nominated representatives of otherwise excluded identity groups; S63 - proportional representation, and requirement for parties to be proportional	A84 - 165/110 FPTP/PR with special minority representation provision; A176 - Provincial legislatures 60/40 FPTP/PR, with special provision for minority representation; A22/223 - local level multi-member
Inclusivity and proportionality	Nil						A19 - right to religious freedoms (less conversions & within tradition); A6 - Nepali as official language, others as national languages; A18 - right to preserve & promote language & culture, and for primary education in mother tongue; A10 - equality, A11 - discrimination ban	A3 - secular, multiethnic etc. state; A5 - all mother-tongues national languages, but official business still in Nepali; A17 right to education in mother-tongue; A2.13.14 - equality, basic rights, discrimination bars etc.; A23 right to religious freedom (qualified); A34&35 - directives for proportionality and positive discrimination	A3 - multieθνic etc. A6/7 provides for multiple national and official languages, Part 3 - standard rights and freedoms; A4 - secular but privileging Hinduism,
Extent of cultural rights and freedoms		A4 - gives some basic freedoms	A15: ban on discrimination; A14: Equality before the law	A4-5: Equality & discrimination bans;	A10, 11 - discrimination bars, equality, freedoms etc.	As per 1962			

Assimilating aspects	Formalized identity based discrimination through Royal Decree	n/a	none specified	<p>A70 - Nepali as national language; A5 - regard to religious tradition & ban on conversions</p> <p>A3 Hindu state; A4 - Nepali as national language; A6 - other Hindu iconography; A8 - ability to terminate citizenship</p> <p>As per 1962</p>	<p>A4 - prescribes as (multiethnic) Hindu state; A6 - Nepali as official language, others as national languages; A27 - king as symbol of Nepal of nationality but adherent of Aryan culture and Hindu religion; citizenship rules have effect that more than 3 million (Madhesis) cannot get citizenship (UNDP 2007: 13)</p> <p>N/a</p>	<p>A4 - ancient religions - i.e. Hinduism - has priority place, and conversions banned</p>
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Annex 3: Indicators of economic growth and nature of the federal states

		A comparative matrix of all federations with comparisons on key indicators											
		Argentina	Australia	Brazil	Canada	Ethiopia	Germany	India	Malaysia	Nigeria	Switzerland	USA	dis and t
GDP/2016	Millions of Dollar.	545866	1204616	1796187	1529760	72374	3466757	2263523	296359	405083	659827	18569100	
Ease of Doing Business	World Bank Group	116	15	123	22	159	17	130	23	169	31	8	business for
Human Development Index	UNDP HDI	0.827(45)	0.939(2)	0.754(79)	0.920(10)	0.448(174)	0.926(4)	0.624(131)	0.789(59)	0.527(152)	0.939(2)	0.926(10)	
Corruption Perception Index	Corruption Perception index 2016	36(90)	79(13)	40(79)	82(9)	34(108)	81(10)	40(79)	49(55)	28(136)	86(5)	74(18)	
Global Competitive Index	World Economic Forum 2016-17	3.81(104)	5019(22)	4.06(81)	5.27(13)	3.77(77)	5057(4)	4.52(39)	5016(25)	3.39(127)	5.81(1)	5.72(2)	
Population Density	World Bank Data		16.02	24.84	3.99	102.403	236.93	445.37	94.92	204.21	211.86	35.32	
Territory	Area in KM2	2736690	7682300	8358140	9093510	1000000	348900	2973190	328550	910770	39516	9147420	

Annex 4: List of Functions of the Federal, State and Local Government

Schedule-5
(Relating to clause (1) of Article 57, and Article 109)
List of Federal Power

SN	Matters
1	Relating to defence and military
	a) Protection of national unity and territorial integrity
	b) Relating to national security
2	War and defence
3	Arms and ammunitions factories and production thereof
4	Central Police, Armed Police Force, national intelligence and investigation, peace, security
5	Central planning, central bank, finance policies, monetary and banking, monetary policies, foreign grants, aid and loans
6	Foreign and diplomatic affairs, international relations and United Nations related matters
7	International treaties or agreements, extradition, mutual legal assistance and international borders, international boundary rivers
8	Telecommunications, allocation of radio frequency, radio, television and postal matters
9	Customs, excise-duty, value-added tax, corporate income tax, individual income tax, remuneration tax, passport fee, visa fee, tourism fee, service charge and fee, penalty
10	Federal civil service, judicial service and other government services
11	Policies relating to conservation and multiple uses of water resources
12	Inland and inter-State electricity transmission lines
13	Central statistics (national and international standards and quality)
14	Central level large electricity, irrigation and other projects
15	Central universities, central level academies, universities standards and regulation, central libraries
16	Health policies, health services, health standards, quality and monitoring, national or specialised service providing hospitals, traditional treatment services and communicable disease control

17	Federal Parliament, Federal Executive, Local Level related affairs, special structure
18	International trade, exchange, port, quarantine
19	Civil aviation, international airports
20	National transportation policies, management of railways and national highways
21	Laws relating to the Supreme Court, High Courts, District Courts and administration of justice
22	Citizenship, passport, visa, immigration
23	Atomic energy, air space and astronomy
24	Intellectual property (including patents, designs, trademarks and copyrights)
25	Measurement
26	Mines excavation
27	National and international environment management, national parks, wildlife reserves and wetlands, national forest policies, carbon services
28	Insurance policies, securities, cooperatives regulation
29	Land use policies, human settlement development policies, tourism policies, environment adaptation
30	Criminal and civil laws making
31	Security printing
32	Social security and poverty alleviation
33	Constitutional Bodies, commissions of national importance
34	Sites of archaeological importance and ancient monuments
35	Any matter not enumerated in the Lists of Federal Powers, State Powers and Local Level Powers or in the Concurrent List and any matter not specified in this Constitution and in the Federal laws

Schedule-6
(Relating to clause (2) of Article 57, clause (4) of Article 162,
Article 197, clause (3) of Article 231, clause (7) of Article 232,
clause (4) of Article 274 and clause (4) of Article 296)
List of State Power

SN	Matters
1	State police administration and peace and order
2	Operation of banks and financial institutions in accordance with the policies of Nepal Rastra Bank, cooperative institutions, foreign grants and assistance with the consent of the Centre
3	Operation of Radio, F.M., television
4	House and land registration fee, motor vehicle tax, entertainment tax, advertisement tax, tourism, agro-income tax, service charge, fee, penalty
5	State civil service and other government services
6	State statistics
7	State level electricity, irrigation and water supply services, navigation
8	State universities, higher education, libraries, museums
9	Health services
10	Matters relating to the State Assembly, State Council of Ministers
11	Intra-State trade
12	State highways
13	State bureau of investigation
14	Physical management and other necessary matters of State governmental offices
15	State Public Service Commission
16	Management of lands, land records
17	Exploration and management of mines
18	Protection and use of languages, scripts, cultures, fine arts and religions
19	Use of forests and waters and management of environment within the State
20	Agriculture and livestock development, factories, industrialization, trade, business, transportation
21	Management of trusts (Guthi)

Schedule-7
(Relating to clause (3) of Articles 57, Article 109, clause (4) of
Article 162, and Article 197)

List of Concurrent Powers of Federation and State

SN	Matters
1	Civil and criminal procedure, evidence and oaths (legal recognition, public acts and records, and judicial proceedings)
2	Supply, distribution, price control, quality and monitoring of essential goods and services
3	Preventive detention for reasons connected with the security of the country, prison and detention management, and maintenance of peace and order
4	Transfer of accused persons, detainees and prisoners from one State to another State
5	Laws relating to family affairs (marriage, transfer of property, divorce, persons on the verge of extinction, orphan, adoption, succession and joint family)
6	Acquisition, requisitioning of property and creation of right in property
7	Contracts, cooperatives, partnership and agency related matters
8	Matters relating to bankruptcy and insolvency
9	Drugs and pesticides
10	Planning, family planning and population management
11	Social security and employment, trade unions, settlement of industrial disputes, labour rights and disputes related matters
12	Legal profession, auditing, engineering, medicines, Ayurvedic medicines, veterinary, Amchi and other professions
13	State boundary river, waterways, environment protection, biological diversity
14	Matters related to means of communication
15	Industries and mines and physical infrastructures
16	Casino, lottery
17	Early preparedness for, rescue, relief and rehabilitation from, natural and man made calamities
18	Tourism, water supply and sanitation

19	Motion pictures, cinema halls and sports
20	Insurance business operation and management
21	Poverty alleviation and industrialization
22	Scientific research, science and technology and human resources development
23	Utilization of forests, mountains, forest conservation areas and waters stretching in inter-State form
24	Land policies and laws relating thereto
25	Employment and unemployment aid

Schedule-8
(Relating to clause (4) of Article 57, clause (2) of Article 214,
clause (2) of Article 221 and clause (1) of Article 226)
List of Local Level Power

S.N	Matters
1	Town police
2	Cooperative institutions
3	Operation of F.M.
4	Local taxes (wealth tax, house rent tax, land and building registration fee, motor vehicle tax), service charge, fee, tourism fee, advertisement tax, business tax, land tax (land revenue), penalty, entertainment tax, land revenue collection
5	Management of the Local services
6	Collection of local statistics and records
7	Local level development plans and projects
8	Basic and secondary education
9	Basic health and sanitation
10	Local market management, environment protection and biodiversity
11	Local roads, rural roads, agro-roads, irrigation
12	Management of Village Assembly, Municipal Assembly, District Assembly, local courts, mediation and arbitration
13	Local records management

14	Distribution of house and land ownership certificates
15	Agriculture and animal husbandry, agro-products management, animal health, cooperatives
16	Management of senior citizens, persons with disabilities and the incapacitated
17	Collection of statistics of the unemployed
18	Management, operation and control of agricultural extension
19	Water supply, small hydropower projects, alternative energy
20	Disaster management
21	Protection of watersheds, wildlife, mines and minerals
22	Protection and development of languages, cultures and fine arts

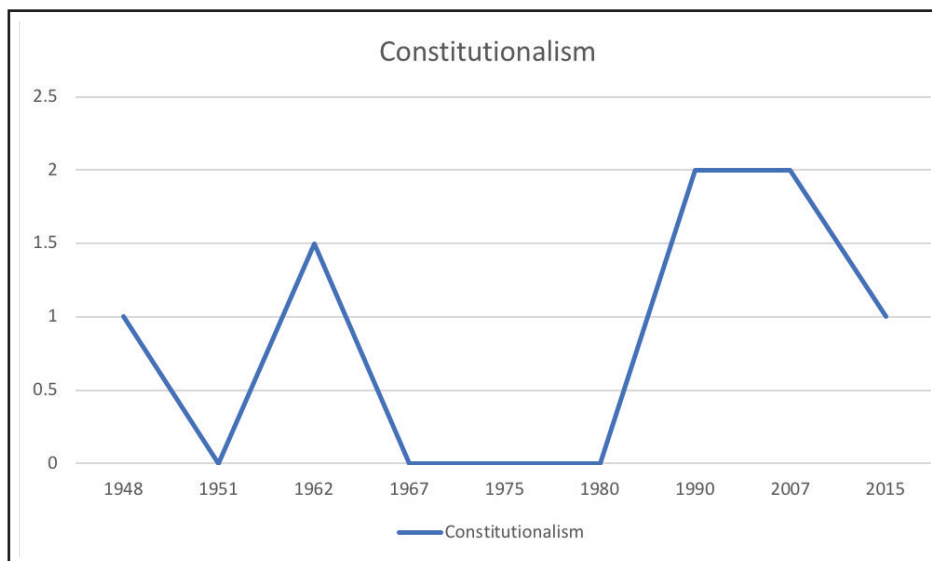
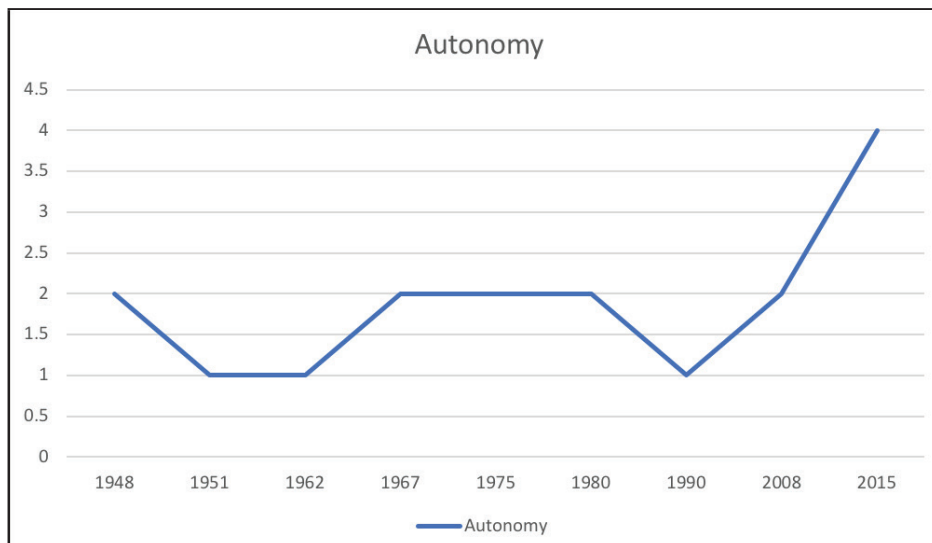
Schedule-9

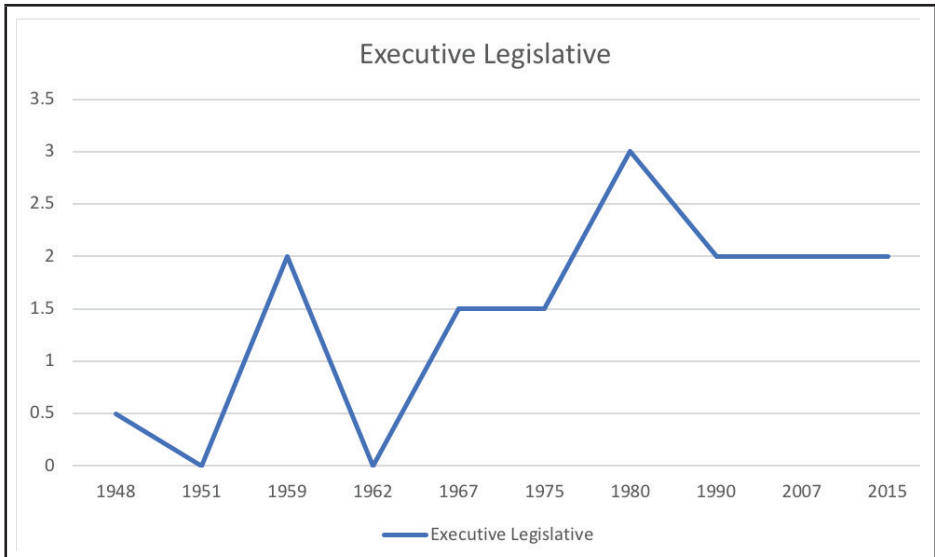
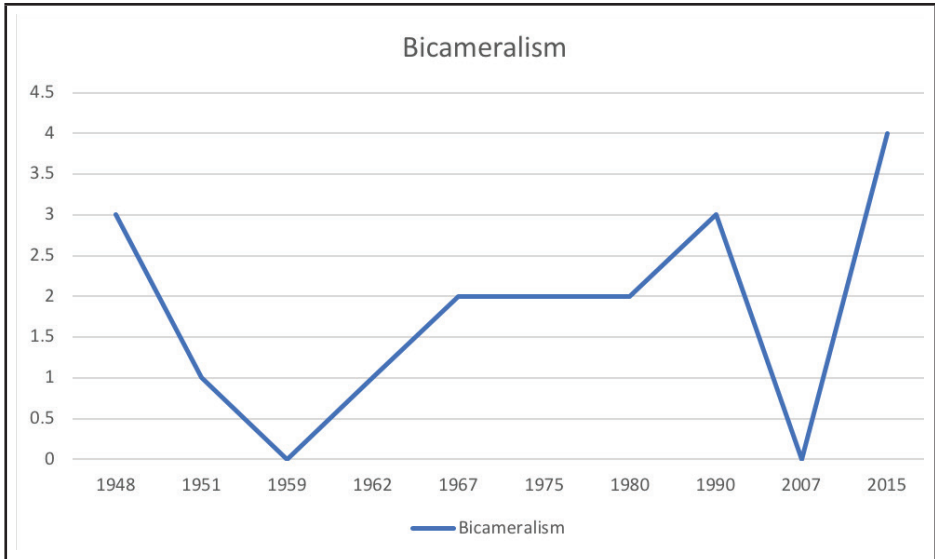
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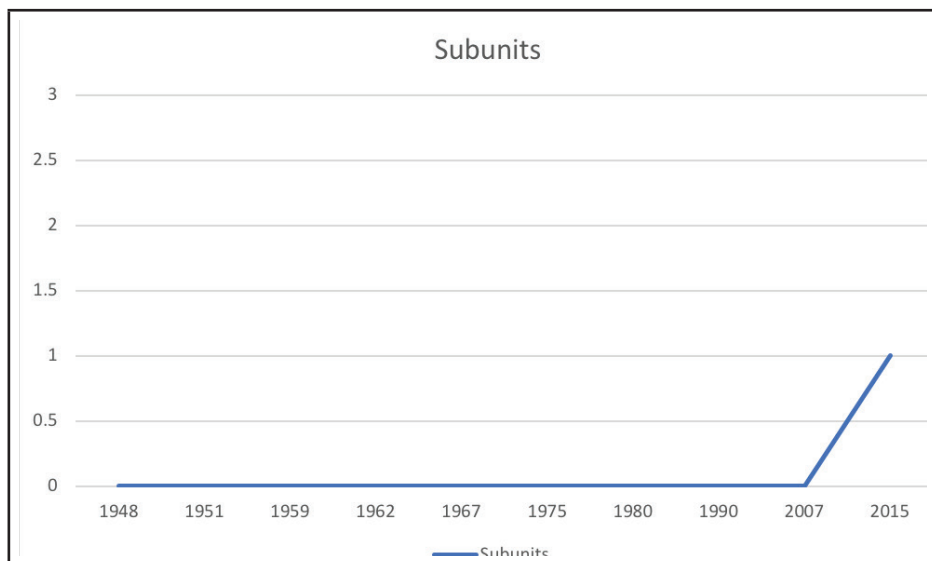
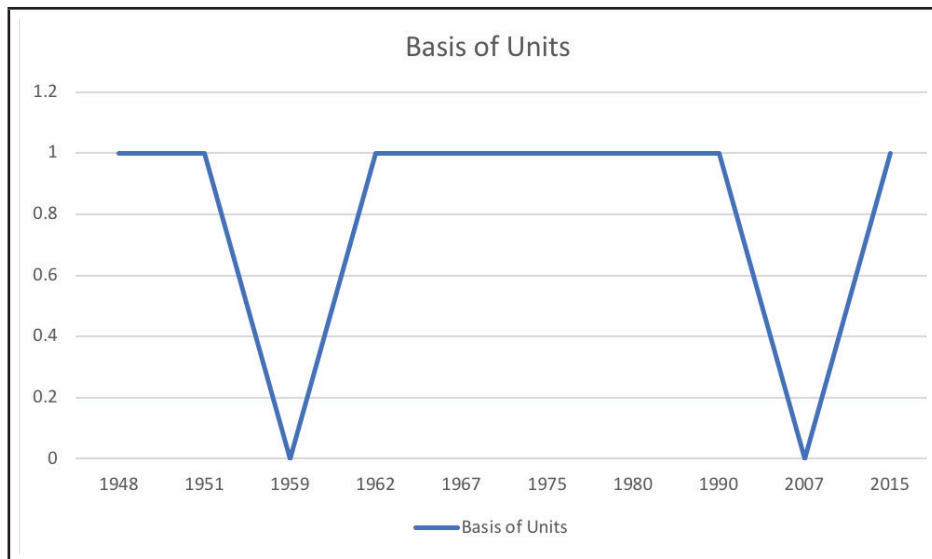
List of Concurrent Powers of Federation, State and Local Level

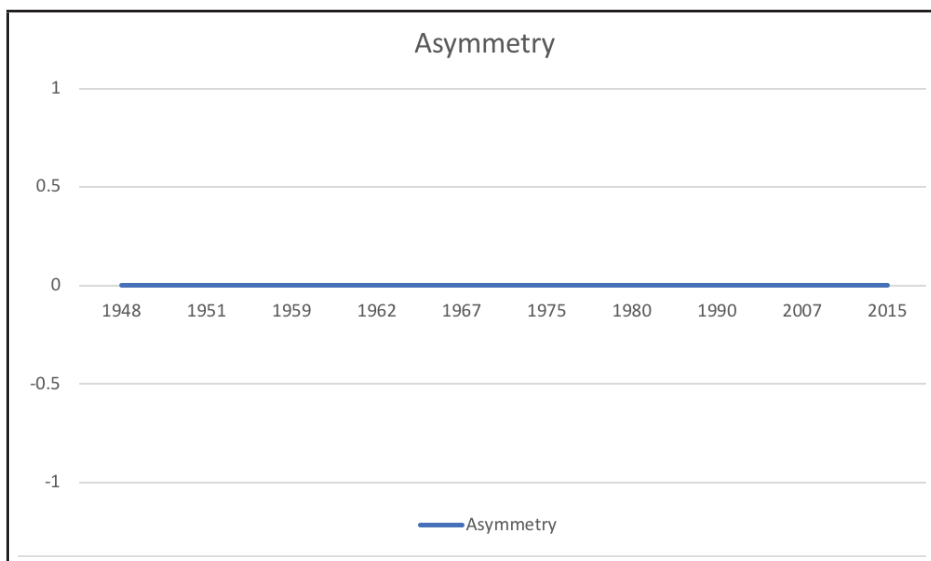
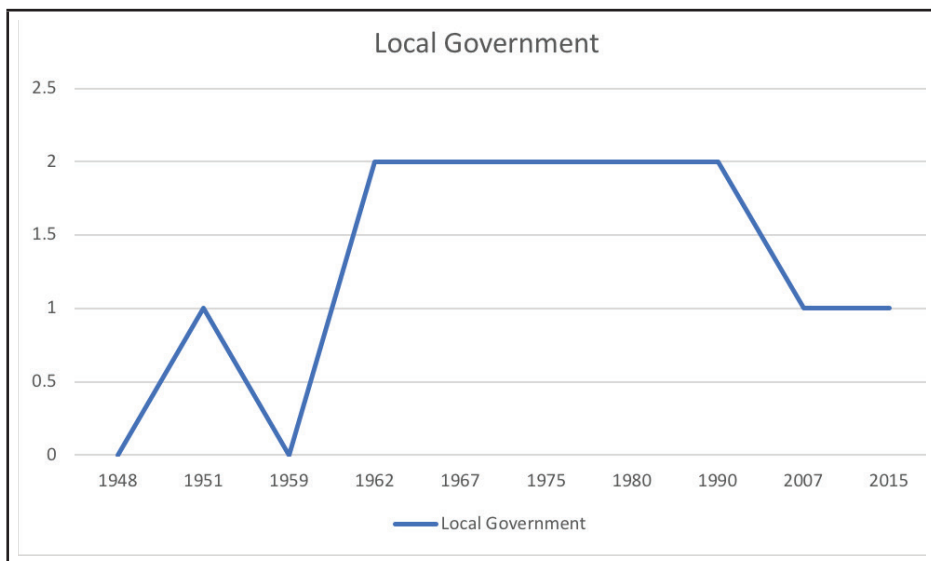
SN	Matters
1	Cooperatives
2	Education, health and newspapers
3	Health
4	Agriculture
5	Services such as electricity, water supply, irrigation
6	Service fee, charge, penalty and royalty from natural resources, tourism fee
7	Forests, wildlife, birds, water uses, environment, ecology and biodiversity
8	Mines and minerals
9	Disaster management
10	Social security and poverty alleviation
11	Personal events, births, deaths, marriages and statistics
12	Archaeology, ancient monuments and museums
13	Landless squatters management
14	Royalty from natural resources
15	Motor vehicle permits

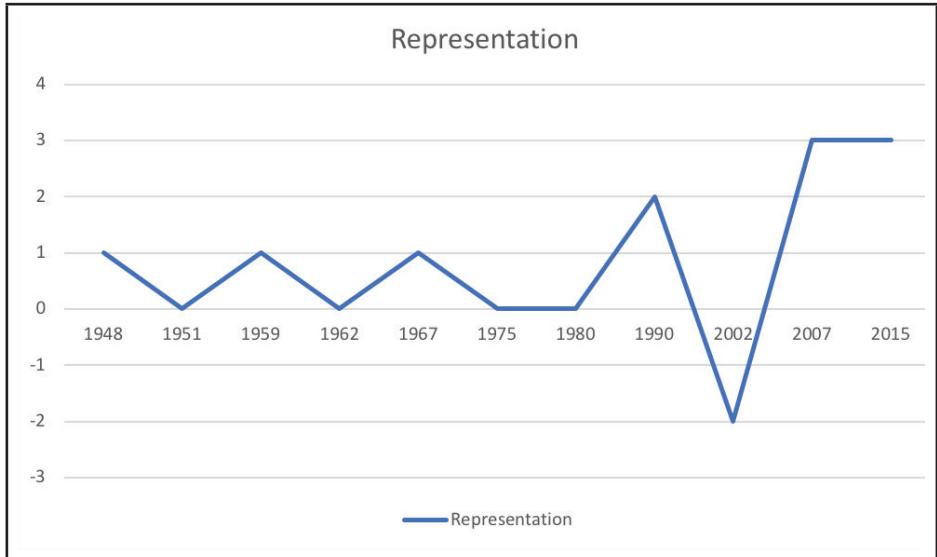
Annexure 5: Historical Trends of Nepal











About Samriddhi Foundation

Samriddhi Foundation is an independent policy institute based in Kathmandu that focuses on economic policy reform. Established in 2007, Samriddhi aims at facilitating a discourse on pragmatic market based solutions for a free and prosperous Nepal.

Known for bringing together entrepreneurs, politicians, business leaders, bureaucrats, experts, journalists and other groups and individuals to make an impact on the policy discourse of Nepal, Samriddhi works with a three-tier approach - Research and Publication, Educational and Training, Advocacy and Public Outreach. Some of its highly successful efforts include the annual economic policy reform initiative named "Nepal Economic Growth Agenda (NEGA)", a sharing platform for entrepreneurs named "Last Thursdays with an entrepreneur" and a regular discussion forum on contemporary political economic agendas named "Econ-ity". Samriddhi also hosts the secretariat of 'Campaign for a Livable Nepal', popularly known as Gari Khana Deu campaign.

One of Samriddhi's award winning programs is a five day residential workshop on economics and entrepreneurship named Arthalya, which has produced over 400 graduates over the past few years, among which more than two dozen run their own enterprises now.

The organization is also committed towards developing a resource center on political economic issues with its Political Economic Resource Center (PERC). Besides this, Samriddhi also undertakes localization of international publications on the core areas of its work. Samriddhi was the recipient of the Dorian & Antony Fisher Venture Grant Award in 2009 and the Templeton Freedom Award in 2011.

More about us at: www.samriddhi.org



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