

INDUSTRIAL ENTERPRISE ACT

..... POLICY BRIEF



SAMRIDDHI
FOUNDATION

Industrial Enterprise Act
:::: Policy Brief ::::

Introduction

The new tabled Industrial Enterprises Bill 2019 is under discussion in the Federal Parliament and yet to be endorsed into an Act. If endorsed, the Bill will become the third amendment to the Industrial Enterprise Act in Nepal. Since the Industrial Enterprise Act was first incepted, it has continuously evolved to facilitate the Industrial landscape of the country. Likewise, the current Bill aims to create investment friendly environment in Nepal, facilitate production of goods and services, create job opportunities, enable optimal utilisation of available resources, promote exports and create a robust economy.

The bill has some positive facets such as the provision of one stop service centre and use of electronic medium for the purpose of registering business and obtaining permits. While provisions like this facilitate businesses and attract investments, there are several provisions in the bill which might have deleterious impact on various industries and overall business environment. On such ground, the brief attempts to identify the shortcomings that are present in the provisions of the bill and make recommendations for amendments accordingly. The shortcomings and recommendation for amendment are subsequently enlisted hereafter

1. Provision for Registration of Industrial Enterprises at Provincial Level

Section	Sub-section	
Section 4	Sub-section 2	Provides provision for Provincial avenues to register and renew enterprises that does not fall under the categories listed on the sub-section 1 of the same article

This provision arranged in this bill is first of its kind after the inception of Federalism to allow registration and renewal of certain category of enterprises at Provincial level, and therefore is definitely commendable. However, the conditions whereby an enterprise already registered at Provincial registration authority will have to also deal with Federal registering authority during certain circumstances will only add compliance requirements and increase amount of time and cost required to fulfil certain legal procedure for enterprises. For instance, enterprises registered at Provincial registering authority will have to retrieve permission from Federal registering authority in apart from fulfilling transfer related nuisance with concerned Provincial authority as per Section 11 when relocating across Provinces. Likewise, such enterprises when expanding across multiple Provincial jurisdictions will also have to get reregistered with Federal Government if previously registered at Provincial authority in order to meet the condition of Clause 4 of Section 4(1).

Recommendation:

Instead, the authority of enterprise registration and renewal should be kept within the registering departments of the Federal Government. And, the issue of access of regulatory

avenues in rather centralizing the entire aspects of enterprise related affairs can be tackled by strategically positioning “the one stop centres” composed of agents representing Federal registration avenues in multiple localities that are easily accessible to enterprises located across the country. Meanwhile, Provincial and local tiers of governments can necessarily assist in effectively positioning and operating such one stop service centre though operated by the representing members of Federal avenues. And importantly, the provision of online registration provided for enterprise registering at Federal department through electronic/digital signature as mentioned in Sub-section 4 of Section 4 can be taken advantage of as an alternative medium to register enterprises.

2. Unspecified time period for conclusion of registration application

Section	Sub-sections	
Section 4	Sub-section 5	Elaborates that the government avenues responsible for enterprise registration shall immediately order the applicants applying for enterprise registration to provide further documentation
	Sub-section 6	Sub-section 6 of the same section of the bill states that the government shall reject the application for enterprise registration with explanation in case the applicants fails to provide the demanded additional documents within the stipulated timeframe

Both sub-sections of the act does not state how many specific days will the registering avenues take in deciding to order the applicants to submit further required documentation or rejecting the application altogether with explanation after the documents have been submitted by the applicants.

Though the sub-section 5 of the section 4 states that the concerned enterprise registering avenue shall “immediately” decide and order the applicants to submit further required documents after receiving the first issue of documents, the use of vague terms as “immediately” can have multiple interpretations, and therefore is open to exploitation by the officers of the registering offices. In other words, such unspecific time limits allow opportunities for registering officers to extend

number of days to fulfil the task on their own discretion, thus compromising the speed of the service delivery. Such anomaly has direct implication on the number of days required to register a business, and therefore affects ease of doing business.

Regardless, the sub-section 1 of Section 5 of the bill states that the enterprise registering avenue should register the enterprise and provide registration certificate with prescribed format within 5 days of application being received with required documentation. However, it is not clear if the sub-section 1 also requires registering offices to demand for further sufficing documents from the applicants or reject the application altogether within the same time limit.

Recommendation

As a resolution, amendment should be made in Sub-section 5 of the Section 4 by providing the provision of specific timeframe within when the enterprise registering avenue should submit further required documentation if necessary or reject the application altogether after it being submitted for the first time. Or, it should be made clear in Sub-section 1 of the Section 4 of the bill that the deadline of 5 days is also applicable for registering avenues in relation to requesting for further documentation or rejecting the application altogether after it being submitted by the applicants for the first time.

3. Unspecified criteria to retrieve permission

Sections	Sub-section	
Section 8	Sub-section 5	Provides authority to the Industrial and Investment Promotion Board (IIPB) established as per section 4 of the same bill to add unspecified further conditions and criteria to approve applications asking for permission to establish enterprises falling under Schedule 1 of this Industrial Enterprise Bill

It can be argued that such discretion to add unspecified conditions and criteria while allowing permission to register enterprises can lead into misuse of authority by the board members. In other words, the board members on their own personal judgment may add unnecessary restrictive conditions for enterprises that do not fall into their favour or opposite for enterprises that do fall into their favour.

Recommendation:

Provisions in terms of limit of conditions and criteria that can be prescribed by the board with genuine explanations should be kept in this bill that prevent the board members from restricting or promoting certain enterprises based on the judgment that does not meet the purpose of the board.

4. Composition of Industrial and Investment Promotion Board

Section	Sub-section	
Section 20	Sub-section 1	Exposes the composition of the Industrial and Investment Promotion Board (IIPB) with ex-officio members.

With the board comprising entirely of ex-officio members, the chances for the board to accomplish their assigned task within the stipulated time period is less likely as the ex-officio status will often hold them with primary responsibilities leaving less time to meet regularly, or timely carry out the functions that they are required to as members of the board. Importantly, such status of the board may not allow them to make decisions regarding whether to provide permission to operate enterprise requiring permission even within 30 days which is required by the bill as mentioned in the Sub-section 4 of the Section 8.

Recommendation:

Instead, the bill should contribute towards fine tuning the composition of the board by at least demanding authorized representing members of the government offices, ministries, or department than summoning Chiefs, secretaries, and governors of the offices whom are mostly engaged in handling the strategic direction of the offices they are primarily responsible for. As a moderate adjustment, at least the core functioning members of the board should be of the status whereby they are primarily responsible for fulfilling the decision-making task of the board even though the chief of the board fulfilling mostly figurative role can still be the Minister of Commerce and Supplies.

5. Need to submit Application to retrieve enterprise records and pay stipulated fees:

Section	Sub-sections	
Section 16	Sub-section 2	Records relating to enterprise registration, renewal, entity transfer, relocation, capacity upgrade, capital upgrade, objective addition or change, or enterprise registration revocation kept securely by the enterprise registering avenue (also in electronic format) can only be made available to the concerned enterprise after receiving formal application
	Sub-section 3	Fees stipulated by the registering avenue should be paid while submitting application for such request

Requiring to lodge a formal application to access such records by paying certain fees stipulated by the registering avenues not only creates an unnecessary procedural hassle for the enterprises but also exhibits a rent-seeking mentality of the government willing to unscientifically extract revenue from the private enterprises. Besides, the elaboration in the sub-section 3 whereby the amount of fees to be levied for such records retrieval be as stipulated by the registering avenue may allow officers of the registering avenues to charge any amount for the service as per their personal discretion.

Recommendation:

Instead, the clauses in the bill should allow authentic documentations and records concerning a particular enterprise to be shared with the owner of the enterprise in electronic format accessible freely whenever required. Such information if required to be transacted securely may also be transacted through the encryption mechanism of digital signature. Nevertheless, access of such records of enterprise details should be fundamental rights of the concerned enterprise.

6. Provision for Sick Industries

Section	Sub-sections	
Section 39	Sub-section 1	Enterprises that have been currently operating at the capacity of 30% or less, and have been suffering net loss throughout the same three years period to be declared as sick enterprise through the specified criteria and by fulfilling the specified procedure for such declaration. Such declaration comes with the condition that the declared sick enterprises have to be operating for at least five years since establishment, and the deplorable state of the enterprise should be purely the result of external circumstances or difficulties not relating to management weakness or their sole intentions
	Sub-section 2	Provides resolution for such declared sick enterprises by arranging provision for them to be provided with unspecified exemptions and facilities in case the scheme or proposal submitted by the management of such sick enterprises, and the investigation carried out by the Ministry of Industry under such enterprises convince that the very enterprises can return to optimal status of operation if provided with necessary exemptions and facilities until certain period.

At first and foremost, the market left to its own devices is bound to evolve continuously and shall lead certain industries and nature of businesses to become obsolete over time. In fact, the rate of market evolution in the contemporary era is likely to make a five years old business model out of favour mostly as a result of market forces introducing innovative business processes and products more adaptive to the consumer's requirement. Illustrations concerning demise of Video Disc retailers and Cyber cafes once popular in the city neighbourhood amid availability of cheaper multimedia supportive personal devices, online video streaming applications, and Home Internet service providers is a vivid case observed in the entertainment retailing industry of Nepal whereby a particular nature of business has been purely made obsolete as a result of change in external or market circumstances.

As such, the provision in the latest Industrial Enterprise Bill to offer financial or non-financial assistance to a crumbling enterprise operating on at least five years old business model just because the cause of its despair is completely independent of management ineffectiveness or their sole intention and only due to ongoing external circumstances shall only lead to spending of government efforts for intervening the dynamics of the market for worse. Such intervention, though carried out with pure intention to support the economy, shall not only lead to unnecessary spending of public money but also deter the market from becoming competitive and efficient. This practice purely goes against the theory of Creative Destruction believed to promote innovation and growth in the economy.

While this provision for sick enterprises in the bill if followed with benevolent intent is not beneficial for the welfare of the self-governing market and the economy of the nation, the

two clauses of the bill detailing the provision is not without loopholes available for exploitation. Firstly, the use of the phrase “as per specified criteria” in Sub-section 1 of Section 39 while declaring a particular enterprise as a sick enterprise even when the clause details that the very enterprise should have come under water purely as a result of external circumstances creates room for the authorized officials of the declaring office to categorize a particular enterprise as sick enterprise based on any criteria that he or she can claim to be a part of the specified criteria which however is not elaborated in the bill. The unscrupulous officer may exploit the clause purely with the intent to advantage a particular enterprise on his or her favour with government sponsored facilities and exemptions that are also unspecified in nature as expressed in the Sub-section 2 of the section 39 of the bill.

Other than not specifying the nature of facilities and exemptions to be provided to an enterprise declared as sick in the Sub-section 2 of the Section 39 of the bill, the very clause also fails to specify the exact time until when the declared sick enterprise shall be privileged with government sponsored facilities and exemptions. As such, it is not only uncertain until what extent shall the taxpayer’s money be deployed in subsidizing the sick enterprises but it is also uncertain until when the unspecified extent of facilities and exemptions be provided to the enterprises that are declared sick on unspecified grounds. Not to mention, such vagueness in multiple areas of the Sub-section 1 and 2 of the Section 39 provides significant opportunities for the officers of the government to unscrupulously exploit the clauses to largely benefit personal favours while also enables the government itself to eternally support its loss-making Public Enterprises through taxpayer’s money.

Recommendation

As a resolution, the updated Industrial Enterprise Bill should not offer privileged provision for faltering enterprises with exemptions and facilities just because their dire status is purely the consequence of external circumstances. The lawmakers concerned about the long-term Industrial and economic welfare of the economy should primarily understand the fundamental principle of free market, and therefore should not promote regulatory provisions that attempt to distort the market mechanism. If it is not practical to completely scrap the provision of sick enterprises in the bill, then the bill should at least be very specific and rigid about the circumstances during when an enterprise is declared sick, the limit and nature of exemptions and facilities to be privileged, and the extent of time until when such privilege can be provided. Such amendments can at least reduce the intensity of the loophole present in this section of the bill for it to be less exploitable in fulfilling personal discretion of the authority at the cost of taxpayer's money.

7. Regarding Mandatory Corporate Social Responsibility

Sections	Sub-section	
Section 54		Requires any cottage, medium or large enterprise transacting more than NRs 1.5 million annually should at least segregate 1% of the annual profit as Corporate Social Responsibility (CSR).
Section 43	Sub-section 7	Details that if any enterprise falling within the criteria fails to segregate the specified proportion of the annual profit towards CSR, such enterprise is liable to be fined by amount equalling 1.5% of the annual profit for the first fiscal year and additional 0.5% to be fined in subsequent years.

In critically observing such directive present in the current Industrial Enterprise Bill, lawmakers should acknowledge the fascinating aspect of market and commerce whereby the dynamics of freely operating market and commerce already tends to offer maximum utility to the involved party that eventually composes the society. The system of the market/commerce is such that the stakeholders involved in the commercial entities, i.e., consumers, employees, shareholders are fulfilled of their needs, resulting to the welfare of the society and economy. In case, there reserves an argument that commercial affairs are not contributing towards public goods or are also creating negative externalities, then there is already the existence of government that is responsible to fulfil such

requirements by scientifically drawing taxes and other revenues from the corporate entities.

Furthermore, the directive of the Section 54 is also not scientific in nature because it holds the provision that the enterprises should submit proportion of their annual profit based on threshold met on transaction volume. Important to recognize is the fact that higher transaction volume does not directly amount to higher profit as the nature of total operating and non-operating expenses incurred as part of the total transaction volume secured may differ for each entity. In fact, it may not be impossible that a particular entity could be making only meagre profit out of substantial transaction volume enough to be discouraged to carry on with the operation if it has to submit even 1% of the profit for philanthropic purposes. In that case, the directive of the Sub-section 7 of the Section 43 would rather hamper the welfare of the society by dislodging an enterprise system that would have fulfilled the needs of the participants of the very society.

Recommendation

The bill should at least be amended by completely removing the Sub-section 7 of the Section 43 that holds provision to levy fines against enterprises that fails to segregate explicitly specified proportion of profit as CSR. Such clause is unnecessarily punitive in nature and discourages the spirit of entrepreneurship. While the provision of Section 54 can be preserved, the criteria in it should be amended in a manner that the provided requirement be related to certain threshold of profit secured rather than transaction volume made.

8. No Provision for registration of Mobile operating enterprise

Section	Sub-sections	
Section 3		Requires an enterprise to be registered by following the registration procedure provided in the bill.

It is no doubt that the section fairly requires an enterprise to be registered by following the registration procedure provided in the bill. However, the issue is not uncovered until we reach the provision whereby the applicants willing to formally register an enterprise requires providing the exact address in where the very enterprise shall be based on. Such provision is witnessed in the Application form (A) provided in the Schedule-2 of the Industrial Enterprise Regulation drawn from the Industrial Enterprise Act for registering all classification of enterprises to be registered at either Department of Industry (DOI) or Department of cottage and Small Industry (DOCSI).

This clause may be subject to discretionary interpretation by the registering authorities as a requirement for enterprises to have a permanent address in order to get registered. And, such an understanding on behalf of the regulators blocks or at least hinders the registration of mobile businesses that are often established at the scale of microenterprise or small business with one or couple mobile capacities. Such mobile enterprises without exact location of operation may be providing any kind of business services, and are a form of process innovation amid prevailing market competition to offer more convenience to consumers in retrieving general services. In fact, mobile businesses are lately seen to be budding in the rural settings of the country whereby mobile grain milling services running

on tractors are revolutionizing service delivery for farmers of the rural agricultural plains. Such concept of service delivery may as well be inspiring aspirant entrepreneurs in urban regions to adopt this business process concept in solving the modern issues of the urban lifestyle. Regardless, businesses relying on such concepts are subject to be denied of gaining legal registration on account of not meeting the criteria for submitting application for registration due to lack of specific business address.

Such rigidity in limiting the nature of businesses that can be formally registered may have denied or shall eventually deny myriad of innovative business products or processes not previously thought of. And, it clearly defies the very purpose of enterprising and industrializing to leverage upon continuous innovations and improvements to benefit the society at large. In this particular case, such rigidity in registration criteria even contradicts the national goal to allow economically vulnerable group of people to uplift themselves through entrepreneurship, as mobile businesses that require minimal capital investment are mostly seen to be the business aspiration of entrepreneurs belonging to such group.

Recommendation

As a resolution, amendment should begin from the authority of this tabled Industrial enterprise bill to expand the horizon of the nature of business that is welcomed in the formal sector of the economy. As for now, offering an alternative to mandatorily require exact location in where an enterprise shall be based on can pave path for the regulators of the Industries and Enterprises to welcome innovative breakthroughs in future. Such amendment can at least be made for the purpose of registering small and micro scale enterprises at the DoCSI as it

is believed to have more relevance to smaller scale enterprises than medium and larger scale ones.

Amending the provision of registration by allowing innovating business ideas to the formal economy can significantly contribute to the economy of the country apart from benefiting the entrepreneurs, consumers and the society at large. As such, the nature of our Industrial regulation should move away from only recognizing enterprising activities that fall within its defined limit to the kind that at least enables business ideas that are likely to bring progress. Only then shall the government can address the issue of informality in the economy allowing more number of entrepreneurs to access growth and award prosperity to the nation.

9. Discriminatory Provision for Large Industries:

Section	Sub-section	Clause	
Section 24	Sub-section 2	(h)	Provides large industries investing one billion rupees and employing more than 500 people with 100 per cent income tax exemption for the period of 5 years and 50 per cent income tax discount for next 3 years.

The logic providing such tax discounts might be to promote the industries producing in large scale and generate higher employment opportunities. However, data from various sources show that most of the jobs in Nepal are created by Medium and Small industries (MSEs). And past empirical studies conclude sizable contribution of MSEs on the national GDP and employment status as a worldwide phenomenon. When the large industries receive tax benefits, it becomes even difficult for small industries within the same industrial sector to compete with these large industries.

Recommendation

As such, either the large industries should be devoid of exclusive exemptions or facilities to be provided to the large industries, or small and medium sized Industries should be provided with similar exemptions and facilities in order to enable them with even footing or platform for competition.



Samriddhi, The Prosperity Foundation is an independent policy institute based in Kathmandu, Nepal. It works with a vision of creating a free and prosperous Nepal.

Initiated in 2007, it formally started its operations in 2008. The specific areas on which the organization works are:

- i. Entrepreneurship development
- ii. Improving business environment
- iii. Economic policy reform
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