

# **Policy Provisions, Gaps, and Practical Constraints in Promoting Small-scale Forest-based Enterprises in Nepal**



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## **Abbreviations**

|         |  |
|---------|--|
| ANSAB   | Asia Network for Sustainable Agriculture and Bio-resources |
| CFUG(s) | Community Forestry User Group(s)                           |
| DDC     | District Development Committee                             |
| DFO     | District Forest Office (er)                                |
| EIA     | Environmental Impact Assessment                            |
| FNCCI   | Federation of Nepalese Chamber of Commerce and Industries  |
| IEE     | Initial Environmental Evaluation                           |
| MEDEP   | Micro Enterprise Development Programme                     |
| NTFP(s) | Non-Timber Forest Product(s)                               |
| WTO     | World Trade Organization                                   |
| VAT     | Value Added Tax  |
| VDC     | Village Development Committee                              |

## Chapter – 1

### Introduction

Promotion of small scale enterprises based on the principles of economic efficiency and individual/group entrepreneurship at the local level has been one of the main agendas brought in by the contemporary developmental paradigm. Developmental economics has recently developed an understanding that the increased poverty, inequality and deteriorating means of livelihood in rural areas are the result of a lack of entrepreneurship, economic inefficiency, inability to participate in the market, and a tendency to produce for subsistence use only (Scherr et al., 2004; Macqueen, 2008; World Bank, 1994; Craig and Porter, 2006). Based on such market-based model of development, donor agencies in developing countries have started to support for formulation of policies, programs and projects to enhance entrepreneurship at local level as a strategy to incorporate rural communities into the scheme of competitive market mechanisms aiming to foster local economic growth, sustainability and access to means of livelihood. However, it is realized that such initiatives have not produced substantial outcomes as expected, and in most cases, entrepreneurship has become a strategy to exploit local resources and promote bureaucratic control over the local production processes (Antinory and Bray, 2005; Marshal et al., 2003; Agbeibor, 2006). One of the main reasons behind such failure is found to be an inappropriate policy environment at policy formulation level and also in its implementation (MEDEP, 2010).

In Nepal, development organizations have promoted entrepreneurship as one of the main developmental themes for the last ten years. The main objectives of entrepreneurship development have been to create suitable policy environment, fostering market linkages and developing entrepreneurial skills at the local level (Subedi et al, 2001; ANSAB, 2009; MEDEP, 2010). For example, Micro-Enterprise Development Project (MEDEP), as one of the pioneer interventions in Nepal, facilitates establishing individual and group-based enterprises at community level in more than 36 districts by promoting entrepreneurial skills, financing mechanisms, market linkages and technology. Such interventions have primary focus on promoting enterprises to produce goods and services for the market using raw materials from agricultural products, forest resources, service providing businesses (shops, restaurants, workshops), dairy products, food processing, etc. Development of forest-based entrepreneurship is one of the main priority areas in Nepal. It is because of an existence of a long history of forest-based local trade and a successful implementation of community forestry for the last thirty years which has generated an enormous amount of forest resources providing diversified raw material base at the local level. Community forestry has already passed through institution building and forest rehabilitation or resource generation stages, and it is now in a stage of utilizing forest products in an effective way so that it generates economic opportunities at the local level. This opportunity of promoting forest-based enterprises has further reinforced by the government's priority of creating green-based local employment, environmentally friendly economy, and local value addition. However, the overall policy environment is not conducive to the promotion of forest-based enterprises locally, and there are numerous legal contradictions between different forests related policy documents and enterprise development provisions. This situation has not only created a gap between actual policy provisions and practices on the ground, but also slowed the enterprise development processes allowing spaces for manipulation, corruption and extra legal difficulties especially due to international standards, agreements and trade regulation mechanisms.

Forest resources are governed by the centralized bureaucracy, and also owned and managed by local community groups and individual households. Multiple ownership provisions of forest resources and centralized bureaucratic authority have created a complex enterprise policy environment or legal systems within the forest sector in Nepal. This is due to unclear policy provisions, contradictions between different policy documents, and difference between policy provisions and practices at the local level. Enterprise development policies are designed favoring big businesses and global corporate sector which is undermining small-scale enterprises managed by rural communities. However, a comprehensive policy analysis is not available in Nepal which could help to change policy provisions and practices at various levels so that the small scale enterprise promotion becomes a mainstream development program.

To fulfill such gap in policy understanding, this paper aims to find out policy provisions, gaps, and contradictions related to small-scale forest-based enterprises in Nepal. Specifically, this research identifies: 1) what are the policy provisions in establishing forest based enterprises; 2) what are the gaps in policy provisions and practices; and 3) what are the contradictions between different policy provisions and actual practices on the ground? Based on the review of policy provisions, hurdles and challenges, a concrete list of recommendations is provided as a way forward in developing a conducive policy environment for the promotion of forest-based enterprises in Nepal.

Methodologically, this research was conducted by interpolating desk review of policy documents with the field level interactions (interviews, focus group discussions, on-site observation) with entrepreneurs, implementers and facilitators. Along with review of policy documents and field visits the necessary information was collected consulting experts on the subject matter and policy making individuals and institutions. A thorough analysis of value chains of four products is conducted – Allo fiber, Resin, and Incense sticks (Kaulo) – to understand specific policy hurdles for different types of enterprises within forest sector. Specific policy issues are documented dividing them into different stages of enterprise establishment and production – registration, collection, processing, financing, marketing, taxing, marketing, etc.

This report is divided into five sections including this introductory background. The second section maps out the overall policy environment, especially the provisions in establishing and managing forest-based enterprises at the local level. The third section will develop a comprehensive analysis of existing policy gaps and contradictions. Such analysis is reexamined by identifying practical policy constraints of three products in section four. The final section provides a list of recommendations.

## Chapter – 2

### Policy provisions for forest-based enterprises in Nepal

Establishment and management of small-scale enterprises are regulated and controlled by a number of policy provisions stipulated under various legal documents and procedural guidelines. The forest-based enterprises require to follow some extra legal procedures and conditions, and therefore it makes the establishment and production processes cumbersome and sometimes inaccessible to poor and illiterate people. The complicated nature of forest-based enterprise policies is due to the availability and extraction of raw materials from different regimes of forest ownership – private, community and government. There are different policy provisions for different ownership systems, which affect each other creating extra legal procedures and steps to be followed. Whereas for other types of enterprises (agriculture, livestock, food processing, etc) the raw materials come mainly from private resources and therefore there are less confusing provisions although the overall policy constraints and obligations are the same. This section maps out a policy landscape focusing on the forest-based enterprises to understand regulatory mechanisms for forest related small-scale enterprises in Nepal. The synthesis of policy provisions are presented under nine main stages of enterprises – registration, collection of raw materials, processing/production of goods, environmental provisions (EIA/IEE), financing, tax systems, transportation/storage, marketing (domestic and international), and revenue distribution (in community-based enterprises).

#### 2.1 Enterprise Registration

Official registration in the Cottage and Small Industry Office is the first step for the establishment of small-scale forest-based enterprises in the district. Government has categorized enterprises into three main groups mainly for the purpose of registration, tax regulation/exemption and financial management – small and cottage industries, private companies, and cooperatives. Registration of one type of enterprise does not prevent from registering another type by the same individuals or the group. There are different regulatory mechanisms and registration processes for each of them, and specific legal documents are enacted separately to define and control enterprise activities.

Registration of **small and cottage industries** is regulated by the Industrial Enterprise Act 1992 and Small and Cottage Industry Procedural Guidelines 2009. Enterprises with less than Rs 200,000 fixed capital and Rs 30 millions working capital can be registered as small and cottage industries in the Small and Cottage Industry Offices in the district. The Industrial Enterprise Act 1992 defines cottage industries as those enterprises which are based on ‘traditional skill or local raw materials and resources, and labor intensive and related with national tradition, art and culture.’ The same Act defines small industries as ‘industries with a fixed asset of up to an amount of thirty million rupees.’ In general, small and cottage industries are understood as a kind of self-employed entities which produce raw materials (for secondary processing) and local consumption goods in a small scale. Most of the micro-enterprises initiated and supported by development organizations fall under small and cottage industry category; nevertheless, if entrepreneurs want to register as company even though their amount of financial investment is small they can register for it. Cottage industries can be registered either as an individual or a group owned categories. If more than two individuals want to run an enterprise locally that can be registered as a group enterprise.



- There are no separate legal procedures and category for the registration of micro-enterprises. They are defined and registered under the legal provisions of small and cottage industries, and they can be registered in the Cottage and Small Industry Office at district level.
- For the registration of forest-based enterprises, the proposal of the enterprise must be approved or permitted by the District Forest Offices (DFO). DFO grants such approval only after the enterprise concerned submits a report on the evaluation of environmental impacts of the proposed enterprise, inventory of raw materials in the given forests and distribution of benefits within and between CFUGs.
- According to the Small and Cottage Industry Procedural Guidelines 2009, the small and cottage industries can be registered within six months of production, and must be renewed in every three years
- The procedure and required documents for registering a micro-enterprise is given in annex-3

**Private companies** are registered in the central Company Registrar's Office in Kathmandu as defined by the Company Act 2006. The main objective of the company is to make profit through organized production, marketing and long term businesses, whereas small and cottage industries are considered as local production and sale for fulfilling everyday livelihood requirements by utilizing traditional skills, raw materials, and local technology.

- A company can be registered with individuals or groups (CFUGs) or both as shareholders. An individual can also register company even though the enterprise is intended to produce goods as defined under small and cottage industry. Choosing an enterprise type could be an issue, but as companies are registered only in Kathmandu, local entrepreneurs (especially the micro-enterprises) naturally choose to register their enterprises locally in the district as small and cottage industry
- Memorandum of association (production proposal of the company) and articles of association (regulation of the company) must be prepared by the proposed enterprise before applying for registration
- The enterprise must not produce and sale goods and services before registering the company if the enterprise is intended to register under the Companies Act 2006
- The ownership of the enterprise can be changed by selling the shareholding capital to another shareholder, whereas the ownership of the enterprises registered as small and cottage industries can be transferred only by transferring the ownership of entire enterprise
- If the proposed enterprise intends to produce and market the produced goods it must be registered as company and also as small and cottage industry. A company cannot produce goods locally if it does not register locally as well. Forest-based enterprises are usually registered in both places so that they can produce and sell goods at national and international levels.

Micro-level production and sale can also be organized under **Cooperatives**, which are registered in Cooperative Division Offices as defined by Cooperative Act 1993. It has more social objectives rather than profit making; however, cooperatives can make profit and divide among their members. The only difference is that certain percentage of its earning must be spend for the general social welfare and cooperative education of its member communities. As it has a social and community approach of organizing like minded individuals as a cooperative group it requires at least 25 members to be able to register as an enterprise under Cooperative Act 1992.

- Micro-enterprises can be registered as cooperatives if there are more than 25 members interested in producing similar goods
- Goods produced under cooperatives are not allowed to export by cooperatives outside the country therefore it is not suitable for those products which are marketed directly by micro-enterprises. The certificate of origin is required for marketing goods internationally, but it is hard to get such letter in the case of cooperatives, because cooperative cannot become a member of FNCCI
- A cooperative cannot be expanded in many places. It can cover maximum of five Village Development Committee (VDC) as its working area
- Initial Environmental Evaluation (IEE) and Environmental Impact Assessment (EIA) must be done before applying for getting approval from forest offices to register forest-based cooperatives. This provision is same for other types of enterprises as well.

Registration of an enterprise is one of the main activities for the local entrepreneurs. A number of policy documents and legal procedures control and define the enterprise registration processes, which are complicated and inaccessible to many micro-entrepreneurs. This has not only made the registration procedure a difficult task to entrepreneurs, but also created confusions in choosing enterprise types, available legal facilities, and benefits in production and distribution. Facilitating institutions are instrumental in this process to help micro-entrepreneurs.

The Industrial Enterprise Act 1992, The Companies Act 2006, Cooperative Act, 1993, and Forest Act 1993 are the main legal documents relevant for registering forest-based micro-enterprises. In addition, Local Self Governance Act 1999 defines the role of VDC as 'motivator' to carry out enterprise activities. According to Forest Act and community forestry directives of the government Community Forest User Group (CFUGs) can register enterprises if it is approved in their operational plan and the authority concerned decides that the group has a capacity to run such commercial production based on raw materials from their forest. The Industrial Policy 2009 has foreseen a strong role of VDC in registering micro-enterprises, fixing location of the factory, and also deciding proximity from the forest. However, such provisions are not legally enacted yet, and therefore the registration of micro-enterprises must follow the provisions made in existing legal documents.

Legal documents related to the registration of forest-based micro-enterprises -

1. The Industrial Enterprises Act 1992
2. Forest Act 1993
3. Forest Regulation 1995
4. Community Forestry Directives 1995
5. The Companies Act 2006
6. Cooperative Act 1992
7. Local Self Governance Act 1999
8. Industrial Policy 2009
9. Micro-enterprise Policy

## 2.2 Collection of raw materials

The collection of the raw materials (forest products) is the second main task for the establishment and operation of forest-based micro-enterprises. Forest Act and Regulations control and regulate most of the raw material collection activities. Raw materials are collected mainly from three types of forests – government managed forest, community forests, and private forests. There are separate provisions, procedures and control mechanisms for each of them.

- In addition to registering as enterprise, a license from DFO is required for the collection of forest products as raw materials from the government managed forests. Forest Act and Regulations define such provisions, and the collection license could be provided only for a part of forests or covering many districts (for example, resin collection). The license should be obtained for each product.
- For the collection of raw materials from community forests the total stock of the products in the forests and the annual harvesting plan of the community forest user group should be clearly mentioned in the CFUGs' operational plan. Such plan should be approved by the DFO. Once the operational plan is approved, the CFUGs can either collect by themselves or contract out to the traders/entrepreneurs for the collection of approved amount of forest products each year. Otherwise the collection of raw materials from the forests is illegal. The enterprise should buy raw materials from community forests according to their operational plan. However, if the collected amount exceeds the minimum quantity for the purpose of IEE/EIA, it is the responsibility of CFUG and purchasing enterprises to conduct evaluation of environmental impacts.
- According to the Forest Act and Regulations, individual can register their forestlands as private forest if they want to sell their forest products in the market. Products from private lands (if not registered as private forests) can only be used for private purpose, but not for the commercial enterprises. The collection of raw materials from private forests should be done only after getting permission/approval from the DFO, and owner of private forest should notify DFO at least before 24 hours of the actual harvest.
- The government has identified a list of vulnerable and rare NTFP species in Nepal which cannot be exported without processing them locally. A few species are banned from collection. According to Forest Act 1995 and Forest Regulation 1995, government may ban the collection, use, sale and distribution and transportation of any forest products. However, as micro-enterprises produce goods locally and do not have better access to export processed goods they tend to sell their collected materials to other processing companies locally. This policy has beneficial impacts to the micro-enterprises because they function as primary raw material collectors and also work for the secondary processing locally (for example, collection of Jatamasi rhizomes for raw oil extraction).

### Relevant policy documents

1. Forest Act, 1993
2. Forest Regulation, 1995
3. Community Forestry Directive, 1996
4. Inventory Guideline of Community Forestry, 2004
5. Buffer Zone Regulation, 1996
6. Environmental Protection Act, 1997
7. Environmental Protection Regulation, 1997
8. Local Self-governance Act, 1999
9. Local Self-Governance Regulation, 1999
10. CITES, 1973

## **2.3 Production/processing of goods**

Quality control is one of the main regulatory controls especially for processing food items and consumable goods that are directly related to human and animal health. There are no specific legal explanations about processing of forest products specifically, but the health and environment related issues in processing are regulated by quality control mechanisms and Consumer Protection Act.

Quality control mechanisms and procedures on processed food items are scattered in many legal documents and provisions – food processing, consumer rights, medicinal products, poisons, agro-products, environmental products, etc. However, these legal documents have focused mainly on health related issues, and do not talk much about managerial and general processing related issues.

- The registered enterprise must secure the Certificate of Quality Standard before it can produce and sale consumable forest products – foods, drinks, juice, etc.
- While processing the factory must not produce health hazardous materials and unhealthy products, and if it produces such lethal materials the enterprise is responsible to compensate the damage caused by the sub-standard (under-quality) products
- At an international level, while exporting forest products, the quality standard of the exported country must be followed. Health related agreement under World Trade Organization (WTO) has banned exporting or importing goods that risk the human and animal health and environment. WTO has developed a standard of producing, packaging, and consumption directions. If such provisions are not followed properly the importing country can ban from selling such products

Apart from quality control measures, Small and Cottage Industry Procedural Guidelines 2009 clearly mentions that the enterprises must develop pollution control mechanism and ensure that the production unit does not damage environmental condition by producing waste, noise, and other pollutants. Appropriate waste and other pollution management procedures should be in place. There should not be any disturbances to the neighbors, and the production/processing operations must not be visible from the main road. This provision can be adjusted according to the nature of the industries.

## **2.4 Environmental provisions (IEE/EIA)**

Protection of the environment while collecting raw materials and establishing enterprises is given a high priority in Nepal's industrial and environmental strategies and legal procedures. This has been one of the strong points if the enterprises are established for the processing of natural resources. Constitutionally, local communities should be given priority for the management and utilization of natural resources. Therefore, the environmental provisions for the enterprises are directly connected to the processing of local raw materials and the ownership of the communities.

Environment Protection Act 1997 and Environment Protection Regulation 1998 are the main legal documents that provide a detailed provisions and procedures in evaluating environmental impacts of the proposed enterprises. These documents clearly state that enterprises which collect raw materials from the forest must conduct IEE and EIA before they operating enterprises and processing raw material. Community forest user groups should conduct such assessment even though their

operational plan explains about the total amount to be harvested annually. There are two ways of conducting evaluating environmental impacts – Initial Environmental Evaluation (IEE) and Environmental Impact Assessment (EIA). The annual quantity of each forest product to be harvested determines which method to be used for the evaluation of environmental impacts.

- IEE should be conducted if the collection of forest products fall under any of the following conditions-
  - 5 to 50 metric tones of roots/root suckers of a single species is collected from a single district annually
  - for the establishment of NTFP garden for the purpose of commercial production
  - for species which require local processing before approved for export, IEE is required if harvested 5 to 50 tones annually in each district
  - extraction of more than 100 cubic meters of sand, gravel, pebbles and soil from the river which flow via forest areas
  - if extracted 10 to 100 metric tones of bark of a species annually
  - if extracted more than 5 metric tones of resin from a district
- EIA is required in the following conditions -
  - if the raw materials come from forests, and processing is done within one kilometer distance from the forest (mainly for resin and turpentine, rubber processing, plywood factory, brick factory, Kattha and timber based match stick factories, pulp industry, cardamom drying, Tea industry, Taxus processing and Incense industry)
  - pollution producing processing NTFPs
  - more than 50 metric tones of roots extraction
  - more than 100 metric tones of bark annually
  - for processing required species if extracted more than 50 tones

However, the regulation mentions that if the enterprises are based on traditional skills and management practices then there are no environmental evaluation restrictions for the collection of raw materials. Micro-enterprises and traditional cottage industries should provide general information on the source of water, and garbage production. But, as a consequence, such production faces difficulties while transporting from one place to another. This is because there is no evaluating agency which verifies such parameters. The identification of traditional industries has become a subjective judgment of authorities. There is no clear separation between traditional commercial production and modern entrepreneurship particularly with regard to micro-enterprise. This has created further confusions among entrepreneurs and enforcement authority.

- A lengthy process of conducting EIA/IEE -
  - preparation of scoping plan and TOR according to the given format in the Environmental Protection Regulation 1998
  - get approval of scoping plan and TOR from the respective department (Department of Forest or Ministry of Environment)
  - conduction of the environmental evaluation, and prepare a report - make it public if it is EIA
  - get approval of evaluation report from respective department or ministry
  - implementation of the report and periodic monitoring

## **2.5 Financing mechanism**

Financing of micro-enterprises is one of the main issues in promoting entrepreneurship in the forest sector. Lack of proper financing mechanism is a barrier for the local entrepreneurs, and most of the existing provisions define loan and investment procedures for the bigger enterprises. In some cases, there are traditional and informal financing mechanisms in which local entrepreneurs can borrow loans from local money lenders. But it has created a different power dynamics and reinforced the feudal type of exploitation. Formal mechanism of borrowing loans is theoretically accessible to all entrepreneurs, but in practice micro-entrepreneurs are unable to produce documents, collaterals and production plan according to the rules of lending institutions. Therefore, most of the micro-entrepreneurs are not funded through banking institutions directly for running enterprises.

Medicinal Plants and NTFP Development Strategy 2001 clearly states that government should provide financial support to the cooperatives for cultivation, collection, processing and marketing. This support does not apply for other types of enterprises, but this provision is not implemented as yet.

- Government has directed financial institutions to invest funds for the promotion of micro-enterprises. Micro-enterprise for this purpose is defined as those enterprises which employs less than 10 manpower and works as an income generating activities locally. The financing mechanisms for such enterprises is called micro-credit
- Bank and Financial Institution Act 2005 mentions that Central Bank can direct any financial institution to provide loans to poor and marginalized communities, and under such directives the concerned bank must provide loans to individuals and communities
- Financial Broker Institution Act 1998 also directs financial institution to provide loans to such marginalized individuals and communities
- Cooperative Act 1992 has a provision of providing loans to its members
- Industrial Policy 2009 has foreseen a system by which micro-entrepreneurs will be organized under cooperatives and provided with a financing loan based on the collateral or guarantee of the cooperative or group from a fund established under Micro-enterprise, Cottage and Small Industries Promotion Board. This policy provision is not in effect as yet.

## **2.6 Tax system**

Tax provisions on commercial production and marketing of forest products are very complicated and inaccessible to the micro-entrepreneurs to be able to get benefits while producing and selling in the market. The overall policy environment shows that government is committed to provide maximum tax benefits to the small and micro-enterprises which produce goods locally and generate employment for the rural population. Nevertheless, as there are too many legal documents (most of them contradict with each other) and complexity in defining and presenting tax provisions, exemptions, and regulations forest-based enterprises are not benefiting from government's intention of promoting entrepreneurship at the local level. Income tax and value added tax (VAT) are two main tax provisions that are relevant for forest-based micro-enterprises.

Industrial Policy 2009 has attempted to clarify the income tax system specifically focusing on small and micro-enterprises although these policies are not formalized as law. This policy has divided rural areas into three main categories – highly underdeveloped, underdeveloped and less developed areas.

Forest-based enterprises established in these areas are exempted for paying tax of 90%, 80% and 70% of the total income respectively for ten years. Industrial policy gives priority to micro-enterprises and proposes that micro-enterprises which produce goods locally should be exempted from paying taxes while buying machinery, raw materials and production materials. It also states that all traditional and cottage industries which are not located in remote areas will be exempted from paying 50% of their income tax. For this purpose the entrepreneur should take a certificate of tax exemption from concerned agencies; however it is difficult to take such document for local micro-enterprises due to centralized mechanism.

- According to Income Tax Act 2001 private companies are not exempted from income tax, whereas small and cottage industries that are established in remote areas are exempted from paying income tax for ten years of establishment. This provision is not defined properly, and there are contradictions with custom regulations and export procedures.
- Self Governance Act 1999 contradicts with other tax regulations and industrial policies of government. It has given full authority to local bodies (VDC, Municipality and DDC) to charge taxes, fees and levy on any kind of enterprise, industry or occupation. VDC and DDC are encouraged to tax on enterprises which extract natural resources. Local bodies can charge tax on all forest products that are extracted within its boundary. These are additional taxes on top of income tax and value added tax. The third types of tax, which is a kind of levy by local bodies (DDC, VDC) – *chungi kar* – is an additional tax imposed while transporting materials from one place to another.
- Value added tax (VAT) is one of the main tax items for forest-based enterprises. According to Value Added Tax Act 1996 all enterprises with more than 20 lakhs of financial transaction per year must register in Inland Revenue Office to get VAT paying number.
  - Enterprises with less than 20 lakhs of transaction are exempted from paying VAT
  - Medicinal plants, its extracts, and artisanal products are exempted from paying VAT. But this legal provision does not define the total amount exempted from paying value added tax. These products can be exported using Harmonized Code 12.11 for the purpose of tax exemption. However, entrepreneurs are paying such taxes in practices due to inconsistent and incomplete definition of medicinal plants and their extract. Harmonized Code is given for *Jadibuti* (medicinal plants) and it does not explain which those items are and what the characteristics to be *Jadibuti* are. This is one of the main contradictions between VAT Act and Custom Regulation.
  - VAT must be paid for when timber is sold either from government forest or from community and private forests (for any amount). Royalty and VAT must be paid if the timber is extracted from government management forest, whereas in community and private forests VAT is charged in no less than government royalty rate
  - If small and cottage entrepreneurs export their products through Export Trading Houses the enterprises can claim rebate for the VAT they have paid for raw materials only

According to Cooperative Act 1993 forest-based cooperatives do not need to pay income tax. However, it is not clear whether such enterprises are required to pay VAT and other taxes or not. Similarly, there is a custom fee for each product if it is exported to foreign countries. Such fees change every year and are different for different products.

Due to lack of legal awareness at local level, enterprises are not getting benefits from tax exemption related policies and laws.

## **2.7 Domestic transportation**

There are many institutions involved in controlling, verifying and punishing enterprises while transporting forest products or forest-based industrial products from one place to another. Among them district forest offices, forest check points and police posts are the main verifying agencies involved in transportation of forest products. Forest Regulation 1995 explains most of the regulatory mechanisms while transporting forest products from one place to another.

- The concerned enterprise should get a release order from DFO for transporting timber. DFO issues such release order after verifying the actual quantity harvested, clearance of the payment and legality of the harvest. DFO officials may inspect harvested timber, saw mills or industries at anytime for this purpose. This provision applies for both timber and non-timber forest products.
- After getting release order the enterprise must inform DFO in advance about transportation date, and it should be endorsed at each check post en route
- CFUG should inform DFO before transporting timber outside community forest user group. Verification in the check post is needed for such timber and other forest products
- CFUGs can issue transportation permit and officially stamp the products with its official logo, however, if there is no any clear provision in Operation Plan of CFUGS to collect the NTFPs from community forestry, the transportation permit should obtain from DFO.
- For the transportation of forest products from private forests the owner should notify DFO in advance along with recommendation letter from VDC or municipality
- Unregistered private forest should get harvesting permits and release order from DFO in advance and endorse in each check post

## **2.8 Marketing (domestic/international)**

Marketing of goods produced from forest-based enterprises is one of the key elements for a successful entrepreneurship. It consists of advertisement, local selling, international export and compliance with the international and exporting countries' rules and regulations. There are no specific legal regulations for the marketing of goods from forest-based enterprises within Nepal. The general customer protection mechanisms and commercial rules apply in forest products as well. Most of the processed and unprocessed forest products produced by micro-enterprises are exported outside the country such as Lokta paper, essential oil, allo fiber, etc. For this purpose there are a number of regulatory procedures that must be followed before exporting the goods.

- According to the Forest Regulation 1995 the exporting enterprise must get a recommendation letter from the concerned DFO to custom office to export forest-based products outside the country
- While exporting internationally, the concerned enterprise must produce the Certificate of Origin, and such certificate is issued by the Department of Industry after receiving recommendation from district chapters of FNCCI and Chamber of Commerce. This kind of recommendation is given to their members only. This provision jeopardizes the cooperatives from getting recommendation letter because the cooperatives cannot be their members, and therefore they are deprived from getting such letter of origin
- Enterprise must also get an Export Permission from department of forest for exporting forest related products before it can be sold internationally



- DFO can grant a permission if the exporting products are not restricted for collection and sell in Nepal and outside
- However, if the products fall under restricted category (banned for collection or requires to process locally before it can be exported), then the producing enterprise must get a letter of approval from the Department of Forest and the Certificate of verification from the Department of Plant Resources
- To export CITES restricted species the concerned enterprise must get a Certificate of CITES from the Department of Forest after the recommendation from the Department of Plant Resources
- Quarantine Certificate is needed to export plant resources outside the country. It is a part of agreements with neighboring and other country for bilateral trade. Such certificate is issued from quarantine check points of Agriculture Department.

## **2.9 Revenue distribution (profit sharing)**

Development programs in Nepal have been promoting entrepreneurship by making use of forest resources as raw materials with the aim of enhancing means of livelihoods in rural areas. Entrepreneurial policy environment is believed to enhance sustainable conservation and utilization of forest resources and increased economic growth. Such assumptions can be true only if the local enterprises managed and run by poor people get maximum benefits and are not exploited as cheap labor for larger companies and rich consumers in the cities globally. Distribution of proper benefits or financial profits to lower producing enterprises (micro-enterprises) from the total value chain of the trade is a crucial point to achieve above objectives.

Unfortunately, there are no regulatory mechanisms which monitor and guarantee the proper and fair share of revenue for small and micro-enterprises. As micro-enterprises are basic producing units (which lack effective marketing skills and accesses) they are the most vulnerable institutions in entire chain of production and trade of forest products. Similarly, there are no clear explanations on how the profit generated from the micro-enterprises should be distributed among the involved shareholders or individuals. This is one of the important aspects of entrepreneurship and enterprise policies which need special attention if micro-enterprises are intended for producing better livelihoods opportunities for the rural population.

## Chapter – 3

### Policy gaps, contradictions, and issues

Forest-based enterprises are regulated by a number of legal documents involving many institutions, enforcement agencies, and national and international policies and practices. As there are so many legal documents, enforcement/support agencies and commercial institutions involved in the process the enterprise development policies in Nepal are full of gaps and contradictions with each other creating practical difficulties at local level. Policy formulation and enforcement is not coordinated among the concerned ministries, each ministry promulgates laws independently and there is not any established practice to see the impact of the proposed policy to different sectors. Such a complex assemblage of enterprise policies has not only created confusions and difficulties, but also provided space for corruption, mismanagement, inefficiency and unbearable exploitation of human and natural resources. This section has identified some of the gaps, contradictions and issues in forest-based micro-enterprise related policies in each stage of enterprise establishment and management. The enterprise policies are focused more on big investment and protection of their interests rather than facilitating micro-level production processes. The overall policy environment is conducive to the big companies, but it is very controlling and hindering for the growth of small-scale enterprises which are forced to follow legal procedures that are primarily enacted for the bigger production enterprises.

#### 3.1 Registration of an enterprise

Registration of the forest-based enterprises is regulated by different legal documents and law enforcement agencies. Unfortunately, there are no specific legal provisions to register the micro-enterprises. They are registered under the category of small and cottage industries. Government has recently developed the micro-enterprise and industrial policies which have a provision for registering micro-enterprises at local level (mostly in VDCs), but these policy provisions are not enacted as Acts and Regulations and therefore there are no micro-enterprises registered under their own category and they are compelled to register as a small and cottage industry or cooperative or company.

The existing legal provisions define and categorize enterprises based on the amount of annual financial investment and transaction rather than ownership structure. The Industrial Enterprise Act 1992 and Micro-enterprise Policy 2008 assume that big investment is not possible at local and community levels, and therefore rural enterprises are defined as small producing units creating self-employed rather than enhancing competitive entrepreneurship. Similarly, the distinction between small and cottage industries and private companies is not very clear. There are no clear definitions and procedures about the involvement of community forest user groups in the companies or other types of enterprises such as cooperative. Companies registered by CFUGs and local individuals are regulated under the legal mechanisms developed for bigger private companies or international firms (corporate sector), and they have to bear similar financial responsibilities and follow similar regulatory control. The involvement of too many institutions in registration and regulation of enterprises processes has not only created spaces for manipulation and corruption, but also emphasized on legal control rather than the actual promotion and facilitation. Some of the major policy issues and gaps related to the registration of forest-based micro-enterprises are as following:

- As there are no separate legal provisions for the registration of micro-enterprises they have to follow registration processes developed for bigger enterprises (such as industry, company or cooperative). Getting approval from DFO, evaluation of environmental impacts, preparation of

the enterprise's proposal in a format developed for other types of enterprises, land title certificates, application in district offices, etc., are some of the main activities which must be followed for the registration of micro-enterprises. These steps are not only cumbersome, but also de-motivating for the development of entrepreneurship among the rural and poor people. Micro-entrepreneurs are not well informed about these procedures and do not get good and proper information as what procedures they are to follow if one wishes to register an enterprise of his/her choice. Likewise government officials' attitude towards the entrepreneur is rather inhibiting and discouraging creating confusion in registration procedures and policy.

- The entrepreneurs must provide an agreement letter between them and the house/landowner to be able to register their enterprises. Generally, the owners are reluctant to sign such agreements because they have to pay income tax if they do so and therefore getting such agreement letter for small scale enterprises is an impractical provision.
- As mentioned earlier, the registration of forest-based enterprises requires a recommendation letter from concerned DFO. Without the IEE/EIA report, DFO rejects to provide the recommendation letter. Small scale entrepreneurs are found unable to afford the cost of IEE/EIA. Additionally, the entrepreneurs must provide the consent from their neighbors which can be an extra hassle.
- There are contradictions between industrial policies and forest regulations on the minimum required distance between forest boundary line and the location of the enterprise. For example, forest policy require that the location of the factory should be at least 3 kilometers away from the forest boundary to produce furniture and veneer/plywood, whereas the industrial policy says this minimum distance should be 1 kilometer or less. Moreover, the distance limit of 2 kilometers in Terai and 1 kilometer in the hills for establishing any type of forest-based enterprises is not practical because it is hard to find such exact location. The decisions of Ministry of Forests and Soil Conservation and Industrial Promotion Board regarding the establishment of forest based industries in industrial estates, district headquarters and municipalities and in areas in Kathmandu valley are contradictory. The Industrial Promotion Board has loosened the distance limit provisions for the forest-based enterprises.
- Entrepreneurs must submit land title certificate (*Lalpurja*) along with the application for the registration of the enterprises. But the landless entrepreneurs don't have such documents and hence, they cannot register their enterprise. Lack of registration hinders them from producing goods in many ways - cannot take bank loan, cannot get electricity and even the transport permission. Targeting such landless entrepreneurs MEDEP has promised to construct a community enterprise building, but such community spaces are not functional at the moment and the landless entrepreneurs face difficulties in accessing such spaces. Construction of community space in public land for is a difficult task because it requires approval from the government agency which is very difficult for the poor people.
- Entrepreneurs who are poor and landless or the others who take land or buildings on lease usually have a hard time in getting consent from the neighbors, which is required for the registration of forest-based enterprises
- There are still existence of old provisions of allocating certain areas to national companies for collection of raw materials denying registration of small and micro-enterprises in the given areas. For example, Ministry of Forests and Soil Conservation has issued permission of Lokta collection from Dhaulagiri zone to Bhaktapur Crafts many years ago. Because of the permission, it is very difficult to register other new Lokta based enterprises for paper making. It is because while registering such enterprises require an approval letter from DFO. But the

DFO doesn't issue the approval letter because of the ministry's permission to Bhaktapur Crafts. Actually it is against the general principles and fundamental concept of industry, trade and marketing, because the constitution has guaranteed of fundamental rights to involve in the enterprise development activities by all citizens as per laws.

- Without registration, entrepreneurs cannot get three phase electricity line from the electricity authority and no registration means exclusion of the entrepreneurs from formal bank loan or other financing supports.
- Registration of a company involving community groups (eg CFUGs) needs fulfillment of extra-conditions than the same nature of company involving individuals. Community groups are not encouraged to take part in entrepreneurial production. The registration processes are designed for individual entrepreneurs and while registering group-based enterprises (groups are shareholders) they are treated as individual entity.
- The different community groups can register an enterprise under cooperatives. However, group membership provisions are absent in cooperative act. Though groups can get share of the cooperative, they cannot become the founder members. This compels them to register under the company act.

#### ***Secured sites for larger companies***

Bhaktapur Crafts has received a license from Ministry of Forests and Soil Conservation to collect Lokta from the government managed forest of Dhaulagiri zone. For an enterprise to be registered, the Cottage and Small Industries Development Board requires recommendation from the District Forest Office. Because of the license, it is very difficult to register a paper factory in Baglung district. Dil Badahur Roka, Production Manager of Himali Handmade Paper said, "We had to struggle hard to register our company. Our products are captured en route to Kathmandu."

#### **Some of the coping strategies of the micro-entrepreneurs -**

- The entrepreneurs become very polite while putting problems before the authorities. They try to convince the staffs that they are doing things honestly and try to do something to improve their economic conditions.
- Instead of dealing with everything during registration, the entrepreneurs employ the consultants or lawyers. They believe that doing things themselves means delay the registration and 'costs more' than the same things done through the consultants or lawyers.
- Registration of an enterprise in woman's name is another preferred option. They believe the authorities are 'less strict' to the women entrepreneurs.
- The entrepreneurs sometime seek support from Federation of Cottage and Small Industries, political leaders or Federation of Nepalese Chamber of Commerce and Industries

#### ***Traders as smugglers***

A veneer and plywood entrepreneur expressed his dismay over the people's attitude. Most of the people behave like the forest related traders were smugglers, and involve into the illegal business, requiring pleasing the local people; donating to the local clubs, schools or health posts. Even the government officials think so; they behave differently to the vehicle carrying forest products. He said, ".....until and unless the government behaves equally with the forest based industries and other industries, the forest based industries will not foster to their fullest swing."

### 3.2 Collection of raw materials

Collection of forest products as raw materials from the forests is one of the most regulated and also manipulated activities within the forest sector in Nepal. District forest offices are the main institutional regulator and forest act and regulations are the main legal documents to deal with the collection of forest products. Most of the legal provisions are very subjective, and are under personal discretion of forest officials creating spaces for corruption, distortion of legal processes, over-harvesting of valuable forest resources, and systematic discrimination against small scale entrepreneurs favoring large scale contractors and business houses. Some of the policy related issues in collecting raw materials from the forests are:

- Government's royalty rate is arbitrary and it does not reflect the actual potential value of forest products and the amount of harvested quantity before they are processed. As the royalty rate does not reflect the market value of the raw materials forest-based enterprises and contractors manipulate with the forest officials so that they get actual market value and officials get the bribe. Fixation of royalty rate for the government managed forests has a direct connection with the selling price of such products from community forests as well. It becomes a basis for them to fix the price from the community forests; therefore, CFUGs are being exploited from alliances of contractors and forest officials.
- Policies on banning collection of some forest products are found to be very arbitrary and unscientific, and have reinvented and institutionalized the informal (illegal) networks of collectors, contractors and forest officials to bypass legal provisions and systematize illegal supply of banned products. Rural collectors (micro-entrepreneurs) are not well informed about the banned species, and therefore they can be exploited by the contractors and traders in taking risks of illegality and ensuring supply in a cheaper way in exchange of fear of information divulge.
- Ministry of Forests and Soil Conservation has agreed and contracted to provide forest resource collection permits of some regions (e.g., district or zone) to the large industries for a long period (e.g., 10 years). Because of this centralized and long term agreement, the local entrepreneurs cannot get collection permits from the district forest office.

The long and 'costly' process involved in getting permits for collection and transportation from DFO has compelled the entrepreneurs to take alternative option. One NTFP collector in Dolakha said, it is easier to transport the products of government managed forest with the permits of community forest user group than getting permits from DFO. It helps us to avoid the officials' trap.'

- As mentioned earlier, Department of Forest has given special permission to collect specific forest products from different large areas to big private enterprises and contractors. On the other side, forest law ensures that CFUGs are legally authorized for fixing the price and selling their products to whoever they prefer to do so. Such double policy standard has created conflicts and also monopolized the market. Exclusive permission to certain companies has undermined the freedom of CFUGs in selling their forest products.
- According to the provisions stipulated in Annex- 2(13) and Annex-1(18) of Environment Protection Regulation, 1998, EIA and IEE should be carried out before handing over the forests to the communities. Due to such

provisions, operational plans of the community forests are not renewed. In such circumstances

community forests cannot provide collection permits of the forest product which eventually invites DFO to issue such permits.

- Harvesting and selling from the private forests as well private farmlands are very discouraging to micro-entrepreneurs. There are so many legal procedures and hurdles that the micro-entrepreneurs who produce goods from private forest resources cannot make profits in real sense as they have to spend a lot of time dealing with administrative processes. Privately owned forest products can be confiscated by DFO authority in anytime. The provisions of registration of private forests in Forest Act, 1993 and Forest regulation 1995 are not clear about utilization and marketing of non- timber forest products from private land. Though the provisions of timber sale and transport are mentioned, the same provisions for NTFPs are absent. This has encouraged illegal collection and trading of the products from the private forests.

NTFP collector and processor reveals that the payment of 5% of the total price of NTFPs to forest officials has been a customary and well established practice in the districts. Once the license is obtained from DFO another payment is needed to satisfy the demands of local leaders, organizations and gangs.

- Forestry regulations clearly mention that there must be an inventory of forest products to determined total stock and annual harvestable quantity prior to get approval for collection. However, there are not developed inventory methods for most of the valuable and marketable herbs/NTFPs, making this provision unimplementable.
- Though CFUGs have rights to issue permits to collect forest products, it is customary to get DFOs' approval. Failure to get such permission makes it difficult to get release order from the DFO. As a result of this process, one prefers to take illegal ways.
- While getting collection permission from DFO, and during estimation of forest products and getting release order, the contractors have to pay 'hidden money' to DFO staffs. In absence of inventory of government managed forest and because of the nuisance of getting permission from DFO, the products are sometimes endorsed as collected from community forests.
- District Forest Office issues collection permit to the contractor. The real collectors (e.g, villagers, poor people, farmers, etc.) don't have the permit. This makes the collector feel insecure. Collectors fear of the officials from district forest office.

Coping strategies of the entrepreneurs in collecting raw materials -

- Entrepreneurs try to please the local people by donating to community development like school, sport clubs etc.
- To be sure of getting raw materials from the collectors, the entrepreneurs make an advance payment to the collectors at the time of festivals (Dashain, Dipawali) or well before cultivating the agriculture crops.
- Entrepreneurs talk about their proposed 'offer' with the forestry authorities and the committee of community forest. This deal makes them easier for getting the collection permit and release order

#### ***Chitrakali's trick***

Chitrakali, an Allo entrepreneur, offered an Allo jacket to forest officer well in advance to 'make herself easy' while getting collection and transport permissions. She said this was her usual 'tactic' to make her business free from operational hurdles that might cost more than the price of the jacket she had offered.

### 3.3 Production/processing of goods

The regulatory provisions on methods and quality of processing or producing goods are very weak for many products. However, this provision is quite strong (although not implemented properly) on the processing of food and health related products. There are many institutions involved in controlling quality of processed food items - Food technology and quality control department, Agricultural quarantine check posts, Nepal quality standard and measurement department, Department of Plant Resources, Medicinal Management Department, and Department of Industry. Although there are many institutions and related legal frameworks involved in controlling quality of the products, the actual quality control is lacking due to lack of coordination among the involved authorities. As a result, there is a compromise in producing quality goods leading to deteriorating marketing practices and consumer interest.

- Not all the forest products especially medicinal plants are tested for its quality and health related issues; therefore, export of such products are always vulnerable to international standard, not because of their bad quality, but because of the lack of quality checking mechanisms and scientific certification processes
- Some species are restricted from exporting before processed locally. But the regulations do not explain what constitutes processing and the necessary conditions to be fulfilled so that such partially restricted species can be exported. This provision has denied the access of micro-entrepreneurs in collecting and trading these species.
- In the competitive market, the products from the entrepreneurs require good label, branding, perfect packaging and also a quality certificate. Though the products of local enterprise are of competitive quality, they are not getting space in the market because they lack support in quality control, labeling, packaging and branding.
- The enterprises producing food items should get license from the Department of Food Technology and Quality Control. It has a centralized system, insufficient labs to ensure quality of the products delaying licensing processes and also creating unproductive bureaucratic hassles.
- Entrepreneurs cope with legal restriction by adapting different strategies. For example, the industries should be established outside municipalities of Kathmandu valley or city areas. But entrepreneurs register such industries outside the municipalities and operate them in municipalities.
- To produce the skilled or trained worker, the entrepreneurs show concerns about the health of the worker, support them in their insurance etc

### 3.4 Environmental provisions (IEE/EIA)

One entrepreneur from Dolakha has amazing experience about carrying out IEE/EIA. He said, 'IEE/EIA is necessary according to the prevailing laws but if you don't get your IEE/EIA by the official of the concerned office it would be difficult to get approval. It is true even if you employ the founder of IEE/EIA.'

Government has developed a number of policy provisions and legal mechanisms to ensure the protection of environmental integrity from the impacts of industrial production. However, most of the micro-enterprises, which are traditional in nature, well integrated with the local environmental conditions, use natural resources that are familiar with the local communities, and are well integrated with the livelihood systems of the people suffer the most from recently enacted environmental protection

mechanisms. Provisions of IEE and EIA are conceptualized based on technical understanding of resource stock or quantity rather than the entire political economy of industrial processes, ownership mechanism, local control and regulation, historical association between forest resources used and micro-entrepreneur communities.

- The legal requirements for conducting IEE/EIA are developed based on the quantity of forest products harvested/collected per year at district level. There are no inventory data for every species collected from each district. There are no any scientific explanations on why specific quantities are fixed for each species as a minimum quantity for such environmental impact assessment. For example, collection of 50 metric tones of roots of a species in one district might wipe out entire available quantity (endangering the availability of collected species) whereas it might be a fraction of total harvestable quantity. The minimum quantities are fixed without a scientific rational.
- Local collection practices, community ownership of forest resources and management systems, local ownership of enterprises, etc are not considered as criteria for determining the evaluation conditions and procedures. These factors might provide more security to the environment rather than quantity of the species alone.
- Fixing district level quantity is unscientific. Each district is very diverse in climatic conditions, and each forest area is unique in terms of environmental/ecological importance.
- The NTFPs and Lokta processing industries should get approval from DFO. Environment Protection Regulation Annex-2 (6) demands EIA of such industry. EIA procedure is too complicated to the small industries.
- To cope with such environmental provisions instead of getting IEE/EIA from independent experts, the entrepreneurs employ staffs of the concerned government office. This saves both time and money. The process goes faster.

### **3.5 Financing mechanism**

Financing provisions are very weak within the government's enterprise development policies in Nepal. There are no systematic provisions, procedures, and practices that provide and guarantee the sources of financial investment to the rural entrepreneurs. Due to the lack of financial resources micro-entrepreneurs produce goods using very basic infrastructure and are unable to expand their production potential.

- Loan provisions to the enterprises are developed focusing on the needs of big industries and investment companies rather than small scale production units. This has created power dynamics between small-scale producers and secondary processors and traders. Micro-enterprises are forced to compete with bigger companies which have better access to financial investment.
- Micro-credits at the community level are not pro-poor; their interest rate is very high and in most cases landless entrepreneurs are denied from getting membership in such credit mechanisms. The existing micro-credit system is not an answer to financing micro-enterprises managed by poor people.
- The banks are reluctant to approve loan to the enterprises/companies if they are not insured by the insurance company. Usually, insurance companies do not sell insurance to the forest-based micro-enterprises and therefore getting loans to them becomes difficult.



- The banking institutions need a detailed production proposal from the enterprises to be able to apply for the loan. The proposal should include the income source, enterprise infrastructure, recommendation from the municipality/VDC, the enterprise space and its boundaries. The bank staffs also make a workplace visit. The small enterprises lack such strength and hence fail to get bank loan.
- There is no legal obligation to financial institutions to provide loans based on group guarantee or individual trust. At present, the entrepreneurs get loans based on the value of collateral presented, and the micro-entrepreneurs don't have sufficient collateral to be able to get loans from the banks.
- At district level, the landless entrepreneurs must provide land title certificate (*Lalpurja*) to be able to apply for bank loans. Even if micro-entrepreneurs get the loan, the interest rate is same as the big business firms. They suffer from the high interest rate.
- At local level, micro-finance institutions are giving emphasis to agro-based enterprise rather than forest-based enterprise, therefore, forest-based enterprise are facing financial crisis to operate enterprise.
- The micro-entrepreneurs can have access to the Nepal Rastra Bank's Rural Self-Reliance Fund, but they cannot have a direct access. They should go through the cooperatives. It means the entrepreneurs should be affiliated to any of the cooperative and Rastra Bank should be convinced to the managerial part of the cooperatives.
- From the inception to return from enterprises, the entrepreneurs require some sort of support. The interest and other operational costs increase every year. So, this is a financially fragile period. Absence of such assurance, micro-entrepreneurs cannot sustain their business.
- As a coping strategy, during the evaluation of the collateral and approving the loan, the entrepreneurs try to please the bank officials. A good relation benefits them.

#### ***Buffalo loan***

Agriculture Development Bank approves loan based on the collateral strengths, the entrepreneurs' goodwill, annual turnover and the stocks and other properties and infrastructure. The small enterprises cannot satisfy bank's requirements to approve the loan. One producer of incense stick from Sindhuli said, 'instead of satisfying the bank's requirement to approve loan for enterprise, we get loan for 'buffalo rearing' and invest it for the enterprises and show our own buffalos to the bank officials.'

### **3.6 Tax system**

There are clear provisions to exempt micro-entrepreneurs and forest-based enterprises from paying different taxes in Nepal. However, as there are so many policy explanations and regulatory institutions micro-enterprises are not benefited from government's policies on tax reduction and promotion of small-scale production. Income tax, taxes by DDC/VDC and value added tax are the main tax items that micro-entrepreneurs are concerned with.

- The Local Self Governance Act 1999 mentions that District Development Committee can collect tax on the forest products if they are imported or exported via its territory, whereas its regulation confuses by saying that DDC can tax on the forest products if they are produced within DDC territory only. This has created contradictions within its regulatory mechanisms,

and as a consequence DDC has taxed all kinds of products that are produced or transported via its district territory. DDC contracts out tax collection task to the private company, and they forcefully collect tax from every kind of product that go through their checkpoints. This is not only policy level contradiction, but also a practical constraint to the micro-entrepreneurs.

- Although VAT Act 1996 exempts from paying tax on exporting medicinal plants and its processed products Custom Act is not very clear about such provisions. The exporters must pay such tax when they export material outside the boarder. There are difference between medicinal plants and other NTFPs, and these differences are not very obvious in custom processes. Custom Act does not explain which products get what kind of exemption for each NTFP. Big exporters are benefiting from this provision, but small-scale producers are unable to verify which products in *Jaributi* and which are not. This is because the term *Jaributi* alone does not explain the names of medicinal plants and what are the contents of exempted materials.
- VAT exemption is only for the medicinal herbs and their extracts, and not for the products mentioned in Annex-6 of Forest Regulation, 1995 (other NTFPs). Since most of the micro-enterprises are producing goods from other NTFPs as mentioned in Annex-6 provision, they have to pay the VAT.
- In addition to the VAT, the entrepreneurs also have to pay the tax over the fee paid to the auditor. Since auditors themselves pay the income tax over the same amount, government is claiming the double tax over the same amount. While paying tax, in addition to the audit report, the tax office requires auditor's signature and stamp in the form. It increased the cost and time in search of the auditor again and again
- Applying for exemption is tedious process and it requires that the enterprises maintain high level of financial records. The micro-enterprises lack proper knowledge about the account keeping system, so they have to rely on the auditors for managing their records. This incurs extra costs for them.
- Though the cottage industries do not have to pay income tax, sales tax and excise duty, the procedure to get such tax exemption is lengthy. One window committee has to decide about such exemption and the department should inform the Inland Revenue office in writing.
- The small entrepreneurs generally cannot understand the tax policy of the government. It is too complex. The provisions of Financial Act (*Arthik Ain*), which change every year, are difficult to comprehend.
- The entrepreneurs get advice from the auditor to know all about the tax exemption and procedure to claim such exemptions.

There are not many Inland Revenue Offices around the country. This has created extra burden to the micro-entrepreneurs. For example, the entrepreneurs from Ramechhap district must come to Bhaktapur to pay the tax.

### 3.7 Transportation/storage

Micro-entrepreneurs suffer the most while transporting forest products from one place to another.

The preparation of various documents before uploading the products and checking, bribing, unloading/uploading and producing documents while transporting are some of the common legal/illegal practices each entrepreneur must follow in this process. Legal provisions are not clear, and the presence and subjective discretion of forest officials, tax officials and police officers becomes law in itself. There are no proper guidelines that are public and knowable to general population, to monitor and control illegality of the forest products while transporting. Therefore, check points and control mechanisms have become a source of illegal activities in itself.

The collection and transportation of Kaulo bark from the government managed and community managed forests are regulated by DFO and respective community forest user groups. However, due to the lack of proper legal provisions, it is very difficult to collect and transport the bark from the private land. Kaulo grows in private farmlands. Private farmers need to show the proof from DFO, which is very hard to get. So, the farmers have to compromise the price and sell the barks to the contractors in the lowest possible price offered by the contractors. Contractors label them as collected from government or community forests and transport them to their factory.

- Regulatory mechanism for the transportation of forest products from one place to another are enforced by too many institutions (forest offices, check points, police posts, DDC, VDC, municipalities on the way, tax offices, custom offices) without a proper coordination and guideline. For example, micro-entrepreneurs have felt that the transportation of NTFPs, mainly medicinal and aromatic plants and products, is impeded by repeated checking at various check posts, even when all the required legal documents are produced. This has been happening either because there are very incompatible legal processes for each enforcement agency or officials are looking for bribe money from the entrepreneurs. The first has become the source for second.
- The overlapping of the jurisdiction of VDC, DDC, police administration, Inland Revenue offices and forest authorities has created repeated tax payment and delays of forest product transportation. Each authority inquires everything. For example, police also inquires whether the taxes are paid or not. Entrepreneurs have to pay taxes to each DDC while transporting via DDC territory. The entrepreneurs must have to pay DDC's road tax. This tax doesn't have separate provisions to small enterprises and big business firm. So, the small enterprises must undergo the same procedure and reduce the competitiveness in transportation.
- The products are not inspected in a single checkpoint. VDC/DDC/Municipalities, police, Inland Revenue and forest offices check the products in different places. This takes longer time and requires additional costs at each checkpoints.
- As the tax on purchasing machinery for small-scale enterprises is exempted in tax laws. But the entrepreneurs have experienced that while getting

Checking of vehicle carrying forest products at police post en route to Kathmandu is another trap for the entrepreneurs. A veneer factory owner said, 'If not satisfied over the money you offer or when you hesitate to pay money, police would ask to unload the products to 'inspect' the vehicle. He will ask to do it no matter how well you assemble the documents /permits and avail them immediately on their demand.'

equipments, tools and machines from other countries, especially from India, the cost of transportation and other unseen cost including money through underhand exceeds the actual machinery cost.

- Policy discrimination exists in transporting agro-based and forest-based juices. Transporting agro-based juices needs no documents but transporting the forest based juices needs approval from DFO.
- While transporting the products, it should be endorsed at each check posts. Vehicles carrying the products have to wait for the staffs for hours. Otherwise the next check post demands endorsement in the earlier check posts. This means that the vehicles need to go back to the earlier check posts and get endorsement.
- The owner of the forest based enterprises needs to stay closely with the DFO staffs, otherwise there would be lots of hurdles. This encourages some hidden practices that incur costs.

Coping strategies adopted by the entrepreneurs -

- The entrepreneurs try to avoid the obstructions of the youth wings of political parties or the members of armed groups by donating money to them

#### ***Tea Expenses***

The entrepreneurs involved in forest based industries have a common practice, known as network making and tea expenses'. It involves making a close relation with the officials and providing some benefits. The police or the forest checkpoints may stop a truck carrying products and demands a visual inspection. This means you unload the products and load it again which costs more. So, the best way to expedite the products is to manage 'tea expense' and go uninterrupted. The 'tea expense' works at everywhere-during taking collection permit, release order, transporting products.

- While transporting the materials, they explain that they run small businesses, use local materials and insist that they deserve discounts. If the police or forestry authorities still stop the material, again they offer some money and clear the way.
- Police inquires about the products transported and might demands visual inspection. At this moment, giving 'some money' simply termed 'tea expense' is the best way to avoid the unloading and loading costs and save time.
- During transporting the products, the traders may find forest checkpoints empty.

So, they have already got a close relation with the checkpoint officials, communicate the tentative time of product reaching checkpoints and so on. The common word for this arrangement is 'making network' which needs some money to operate it

### **3.8 Marketing (international)**

Marketing of the forest products in an international market is almost impossible for micro-enterprises due to complicated export regulations of forest products, small quantity of production, lack of access to buyers in an international market, lack of quality standard, and bribe seeking attitude of the government officials. Legally, they are discouraged from trading goods internationally by creating legal systems in which small enterprises lack capacity to comprehend exporting procedures. It is this reason that the micro-enterprises are paid relatively less in comparison to the total values the forest products. In reality, micro-entrepreneurs are treated as labor intensive workers rather than 'entrepreneurs'. Overall, the policy environment for forest-based micro-enterprises is control oriented rather than facilitative for the access and promotion of market at national and international levels.

- The paper work for exporting forest products are beyond the capacity of micro-entrepreneurs. They cannot deal with different departments, producing various certificates and fulfilling national and international criteria. These provisions are intended for the big business companies who can influence and control forest related trade and export. Micro-enterprises are not considered as entities which can and should produce and market their goods by themselves. As a consequence, micro-enterprises are not developed as a competitive business system, but rather a primary processor for the exporting companies.
- The entrepreneurs must be updated about the changes of the standards of the importing countries and international quality standards. Little knowledge about such standards costs high when the products are rejects at the destinations.
- It is a tedious and lengthy process to obtain the export documents like the phyto-sanitary certificate, and the permission from the management authority (Department of Forests) and the scientific authority (Department of Plant Resource) for the products obtained from CITES listed species. Normally, it incurs additional hidden costs through many underhand tactics.

#### ***Dipping rods***

For the export of essential oil, an exporter said, ‘the container must be sealed off by the department of plant resources before it can be moved to the export outlets. If the officials of drugs abuse control cell of home ministry are not ‘pleased’, they break the seals of those containers and ‘inspect’ by dipping and smelling a rod. Dipping the same rod into different containers damages the quality of the oil. Moreover, once the seal is broken, cargos never accept the consignment. So, to avoid such risks, I feel comfortable to allocate ‘some money’ than getting the oil contaminated.’

### **3.9 Revenue distribution (sharing of the profit)**

There are no any clear policy provisions or legal mechanisms to ensure equitable distribution or fair share of financial profits in the total chain of production and marketing of forest products in Nepal. Micro-enterprises are encouraged to produce goods at local level, but are not facilitated and legally protected from getting proper benefits from national and international marketing. Usually, they are paid less and treated as raw material collectors rather than competitive segment of the market. The distribution of the profit within the members of enterprises (in case of multiple ownership system) is not clear. If communities are managing the enterprises, the poor and illiterate members of the communities are found to be deprived from benefiting financially. Community forestry guidelines have attempted to explain ways to distribute in an equitable way, but community-based enterprise policies and legal mechanisms are unaware or reluctant to the necessity of such policy provisions.

The benefit sharing mechanism are different in company, cottage industry and cooperative and it is generally define in the memorandum, regulation, by-laws or scheme of these types of enterprise. The local enterprises have confusion to choose appropriate types of enterprise for equitable benefit sharing, due to lack of facilitation from government agencies.

There are very high price fluctuations while selling the forest products to the suppliers; therefore the producers are paid from the bottom level of the fluctuated price at all time. One of the reasons for this consequence is that many producers produce small quantity of products, which leads to less payment and lack of control over business processes.

## Chapter – 4

### Policy hurdles in certain value chains

The general policy environment might affect different value chains or forest species differently while collecting, processing and marketing by forest-based enterprises. Micro-enterprises are producing goods from various tree and NTFP species and such variations are not considered while designing and implementing micro-enterprise related programs, policies and laws. However, the analysis of three value chains reveals that forest-based enterprises have been facing similar policy constraints and legal barriers irrespective of difference in traded species or value chains. Allo, resin and incense sticks were studied to identify some of the major policy constraints specific to these products with the aim of understanding enterprise related policies and practices in a comprehensive way. Some of the main policy issues for each product are as follows:

#### 4.1 Allo

Allo is one of the highly commercialized forest products in the mid-hills with the involvement of more than 8000 collectors in total (MEDEP, 2010). As it covers more than 20 districts, and most of the collectors/processors are illiterate rural people thus the policy provisions and legal procedures are not accessible to rural entrepreneurs. According to the collectors, producers, and traders it is almost impossible to follow all the legal requirements for the production of Allo fibers and textiles. Most of the policy provisions are impractical and do not match with the real practices on the ground.

- Collection and processing of Allo fibers are done using traditional methods as an everyday activity of rural people rather than following the government's procedures of licensing, permit taking, inventory of resources and assessment of environmental impacts. Traders and secondary processors buy from such primary producers. This indicates that the legal provisions are not implementable in real life. While exporting to the international market Allo traders follow export related rules and regulations by producing documents using fake information.
- Environmental standards, conducting IEE and EIA, are irrelevant to this product. This is because:
  - it is grown annually and if not harvested on time decays completely in the winter
  - harvesting of Allo fibers does not require uprooting the plant, which means it can be harvested as normal grasses
- The collectors do not conduct any environmental evaluation, however it is done by exporter if the exporting quantity exceeds given amount from a district
- As there is no clear record keeping system in the district, and there are many sources of supplying Allo fibers for the contractors, they can easily escape the environmental evaluation processes.
- Government policies are inattentive to develop a comprehensive information system about the price and other market related issues. Micro-enterprises are especially deprived from such information. This has negative impacts on Allo production and marketing at the micro-enterprise level. Micro-enterprises produce fibers and sell it to bigger contractors. Micro-enterprise policies and practices are not creating an environment by which micro-entrepreneurs get complete information and achieve higher level of financial benefits.
- CFUGs are selling Allo fibers either by allowing its members to collect it and sell individually or can collect and process by itself and sell it to the secondary processors

- Institutions that are involved in regulating forest-based products are all involved in collection and processing of Allo fibers as well, but there are certain copying strategies that entrepreneurs have adapted:
  - establishing collection points in different places based on the informal networks and connections where products from different areas or districts are gathered
  - as there are many collectors and local contractors the actual amount collected annually is hard to determine. There are no proper recording systems at the local level.
  - rather than following all the rules and regulation for collection, processing and transporting to market centres such as Kathmandu, entrepreneurs prefer to pay a little bit to DFO personnel, checkpoints and also to police posts
  - bus drivers are the key elements in making this business possible for most of the local traders. Entrepreneurs send their products by bus in small packages on a regular basis so that there are no evil eyes on their products on its way to market centre i.e. Kathmandu
  - in many instances allo fiber is traded in barter terms locally with the good they require from the market. This has supported the financing mechanism of Allo enterprises. Some of the Allo fiber buyers own their own shops (they are always located in the local towns or nearby roads) or they arrange such goods from nearby shops.
- There is no quality control mechanism therefore it has not only undermined the market potential but also made unaware about the hazardous impacts of using chemicals in cooking and cleaning fibers
- It is seasonal-based enterprise for local peoples, therefore, there is lacking of well established systems and practices for marketing of the product, but local peoples have good indigenous knowledge for collection and processing, however it is not recognized in policies and laws. Therefore, it is require making procedural guideline for documentation and recognition of traditional knowledge on Allo.

## 4.2 Resin

Resin collection is one of the widely implemented forest-based activities in lower hilly areas. Resin collection is done by the processing companies with the special permission from the department of forest and mobilization of local labor. In community forests, resin is collected either by bigger processing companies in a contractual basis or through the CFUGs' networks and its own structure. Resin factories are relatively bigger forest-based enterprises in Nepal, and they have established strong relationship with forest officials to make the collection processes compatible to their industrial needs. Resin collection is one of the perfect examples to illustrate a successful informal alliance among companies, forest officials and local leaders to systematize collection, corruption, and guaranteed supply of collected resin. Most of the resin collection and processing companies are bigger in size. Although bigger in size and scale of operation, they have been facing similar legal difficulties as other NTFP producers and traders. For example:

- Department of Forest issues resin collection permits to few resin production companies. At the same time, these forest areas are handed over to the communities as community forests. This has created a kind of dual ownership causing series of confusions and conflicts among the forest officials and CFUGs.
- DoF is also issued the collection permits to many companies in the same districts or areas and there are many conflicts between these companies for the capture of resin by force or illegally.

- The entrepreneurs feel that the resin collection is not easy when the big chunk of pine forest is divided into many community forests. It is because all the community forests must have consensus over collection of resin which is a lengthy process, and sometimes impossible in the present political debacle.
- The NTFP policy suggests for a good harvesting practice. However, it does not explain about the criteria and methods of a good harvesting practice. The pine trees below 36 inch diameter should be excluded from the resin taping. But in practices trees above 30 inch diameter are also tapped.
- In spite of fulfilling all the legal requirements, the entrepreneurs must please the political parties, local leaders, and forestry officials to make the collection, transportation and processing effective and uninterrupted. For example, an official of HPPCL, a government owned resin Production Company, admits that they must pay at least 15% of the total price to various individuals as a bribe to be able to collect and process resin in their factory.
- The IEE procedure is also lengthy, and costs much. So the community forests are not always prepared to carryout IEE. This ultimately discourages resin tapping though the trees are planned to be taken out.
- The entrepreneurs prepare all the export documents like the bills, certificate of origin etc. Still they have to spend some money for custom clearance.

### 4.3 Kaulo (incense sticks)

Kaulo is used for the production of incense sticks and are mostly collected from marginal forests and private lands. Barks are collected from standing trees and the collection can be done next year from the same tree. However, this product faces exactly similar issues to that of resin and allo while collecting, processing and transporting from one place to another.

- Getting collection permit and release order from DFO is both lengthy and also involves some costs.
- The contractors get the collection permit, not the actual harvester. So, the Kaulo collectors are always in fear about their job because they do not possess collection permits.

#### ***The Fate of Private Forest***

*Legally, forest products like Timur, Lapsi, Kaulo, Allo, etc from private land do not need to pay government taxes. But the owner or the trader has to show documents that they are privately owned. Until you officially register the private forest in DFO, you don't have such documents. It is also not feasible to register the forests producing small amount of products. So, they have to pay taxes as though the products are taken from the government or community forests. The owner of Shanti Agabatti Udhyog said, '...Forest Regulation, 1995 is not clear about how the non-timber forest products in private land should be harvested/transported. Due to this, bulk of products from private land is difficult to transport. So, the farmers either carry themselves in small amounts or sell to the contractor.'*

- The amount to be collected depends upon the personal knowledge of the contractor or the forest official. The actual inventory to estimate the quantity of Kaulo bark is not carried out.
- The provisions in Forest Regulation regarding Kaulo collection from the private lands are not clear.
- Kaulo bark from private land is collected and transported as if they are collected in public land; all the taxes are paid accordingly. Even though all the transport documents are in place the traders have to spend extra money in different check posts.



## Chapter - 5

### Recommendations

This study reveals that the overall policy environment is not conducive to the micro-enterprises and is not facilitative for the promotion of entrepreneurship at the local level. Micro-enterprises are not legally recognized, and therefore they are not promoted as competitive commercial entities, rather they are treated as ‘raw material collectors’ for ‘actual’ business enterprises (corporations at national and international levels). If the local entrepreneurship, competitiveness, commercial production, efficiency and the market are still believed as valid tools for development then the organization such as MEDEP should strongly focus on creating enabling policy environment at various levels based on its long experience in establishing micro-enterprises on the ground. For this purpose, MEDEP should create a separate unit within its structure to facilitate the policy formulation processes and bridge between field level experiences and actual policy writing at the center. Some of the main recommendations for the improvement and creation of enabling policy environment for the development of micro-enterprises are as following:

1. Enterprise related policies are not accessible or easily available to the local entrepreneurs therefore the micro-entrepreneurs are unaware of most of the constraining and also favorable policy provisions. MEDEP is highly recommended to either train or create local level institutions (at least at the district level) which support micro-enterprises in terms of providing legal services in an effective way. A clear, transparent and accessible system should be in place where the entrepreneurs can be informed in advance about the legal/operational procedure and documents necessary for each stages of the business-from raw materials collection to the final product export.
2. There are no separate legal procedures and category for the registration of Micro-enterprises. They are defined and registered under the legal provisions similar to small and cottage industries. Given the scope and objectives of micro-enterprises they should be registered by VDCs and informed to district cottage and small industry offices for information. MEDEP has a very high potential to work on this issue to help government to enact the registration policy at local level.
3. To avoid the nuisance, delay and possible corruptions, a system should be developed in government authorities where entrepreneurs deposit all the required documents to the designated office which will then be circulated to authorities concerned for further action and approval. For example, to get approval or recommendation from DFO should be the responsibility of the Small and Cottage Industry Office once the micro-entrepreneurs apply for the registration.
4. The Industrial Policy 2009 has foreseen a strong role of VDC in registering micro-enterprises, fixing location of the factory, and also deciding proximity from the forest. However, such provisions are not legally enacted yet. There is a need for a separate legal provision (law) that defines clear procedures of establishing forest-based enterprises with the regulatory control of VDCs.
5. The house or land owner is reluctant to make a contract agreement and lend it to the micro enterprises in fear of paying income tax. It is very small amount, but as per the law they must pay income tax if they lend their property to enterprises. This has created difficulties to the

micro-entrepreneurs. Therefore, it is strongly recommended to exempt land owners from paying income tax if they lease the land/house to the micro-enterprises.

6. Ministry of Forests and Soil Conservation provides resource collection permits for some regions (e.g., district or zone) to the large industries. Because of this long term agreement, the local entrepreneurs cannot get collection permits from the district forest office. These centralized mechanism of contracting certain areas and products to specific companies must be scratched for the development competitive entrepreneurship at the local level. MEDEP has field experience and evidences to work on this issue, and it needs an urgent attention from the government and support institutions in the context of growing community forestry in all over the country.
7. The forest act and regulations do not explain about the collection of forest products other than the timber from the private land. This has created space for manipulation and corruption therefore a clear legal explanation is required for the promotion of forest-based enterprises using the resources from the private lands.
8. The collection and trade of timber in private land is fully controlled by the DFO, and it is a tedious process. To simply this process the authority for regulating timber and other forest product extraction for the purpose of processing in local enterprises should be delegated to the local bodies mainly to VDCs in consultation with concerned local forest officers (range posts).
9. The registered enterprise must secure the Certificate of Quality Standard before it manufactures and sale consumable forest products – foods, drinks, juice, etc. However, the lab services are available only in Kathmandu. Therefore, each district level Small and Cottage Industry Office should provide a service of collecting samples from the entrepreneurs, transporting to the labs in Kathmandu, testing the samples, and reporting back to the entrepreneurs. MEDEP should help to establish this mechanism at the initial stage. Similarly, as the micro-enterprises cannot afford the services of the technical personnel like food technician, or other experts. The development organizations should get the support of the technicians for assuring quality production and to fulfill quality standards.
10. For the registration of forest based industries, the entrepreneurs should show the approval of District Forest Office to establish the industry. DFO only provides such recommendation after submitting the IEE/EIA reports as per Environment Protection Regulation. The IEE/EIA process is very complicated and expensive for the local level entrepreneurs. The IEE/EIA provisions should be exempted for the micro-enterprises.
11. The responsibility of conducting the IEE/EIA should be of DFO. The environmental evaluation conducted by the entrepreneurs themselves may not be reliable as they do not have required technical capacity. DFO office itself should be a repository of information and serve as a reference point for information related to EIA. It should be the responsibility of DFO to make EIA in entire district. Moreover, for the forest based enterprise, according to the law, IEE/EIA should be carried out by the resource owners themselves, not by the entrepreneurs. Enterprises only buy the raw materials from the forests therefore should not be engaged in conducting the IEE/EIA by themselves
12. As the loan provisions are not favorable to the micro-enterprises there is a need for a VDC level funds that finance small-scale enterprises locally. This fund can be tied up with the VDC budget system and support the targeted community (e.g Dalits, women etc). Donor

organizations and development programs can provide initial seed money and help to develop system locally. This will enhance entrepreneurs' access to finance. Such local funds do not need property as collateral and can create provisions to approve loan to the enterprise in a group's guarantee, commonly known as 'group collateral' basis.

13. Legal provision for the insurance of tree species and few commercially valuable NTFPs is require for the promotion of forest-based enterprise at local level.
14. Though VAT is exempted for the herbs and its extracts, the VAT Act has not included products listed in Annex-6 of Forest Regulation 1995 like Allo and Lokta. So, VAT may be imposed to these products. Therefore, micro-enterprises should get tax exemption irrespective of their nature of production. Similarly, the medicinal plants, its extracts, and artisanal products are exempted from paying VAT. These products can be exported using Harmonized Code 12.11 for the purpose of tax exemption. Harmonized Code is given for Jadibuti (medicinal plants) and it does not explain which those items are and what are the characteristics to be Jadibuti.
15. Micro-entrepreneurs should be exempted from paying DDC levy (chungi Kar). The provision for this kind of levy is for those products that are exported from the district and marketed internationally. However, DDCs are taking the tax to every product leaving the district. This practice should be stopped for the promotion of micro-entrepreneurship at the local level and help them to link with the national market.
16. Forest based cottage and small enterprises should get uninterrupted transportation to the districts once their products are checked locally in VDC. All agencies or offices related to checking of forest products should establish in one place and operate in an integrated way.
17. Due to the poor labeling, packaging and branding, the genuine products of the small enterprises are not getting attractive consumer preferences. So, the enterprises should get support from the government and non-government organizations in labeling and packaging. It helps them to enter into the present competitive market. Laws on group labeling is necessary to get benefit and access in the market for micro-enterprise

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## Annex-1

### Policies and Government Organizations Relevant to Forest Based Enterprise Development

| SN | Stages                  | Laws and Policies   | Concerned Agencies/<br>Organizations   | Remarks<br>(role)  |
|----|-------------------------|---|--|--|
| 1. | Registration            | <ul style="list-style-type: none"> <li>The Industrial Enterprise Act, 1992</li> <li>Industrial policy, 2010</li> <li>Micro-enterprise policy, 2008</li> </ul>   | <ul style="list-style-type: none"> <li>District office of Cottage and Small industry</li> </ul>  | Registration   |
|    |                         | <ul style="list-style-type: none"> <li>Cooperative Act, 1992</li> </ul>   | <ul style="list-style-type: none"> <li>Office of Cooperative Division</li> </ul>   |  |
|    |                         | <ul style="list-style-type: none"> <li>Company Act, 2007</li> </ul>   | <ul style="list-style-type: none"> <li>Office of Company Registrar</li> </ul>  |  |
|    |                         | <ul style="list-style-type: none"> <li>Joint venture (Sajhedari) Act, 1963</li> <li>Private Firm Registration Act, 1957</li> </ul>  | <ul style="list-style-type: none"> <li>Department of Industry</li> </ul>   |  |
| 2. | Raw Material Collection | <ul style="list-style-type: none"> <li>CITES, 1973</li> </ul>   | <ul style="list-style-type: none"> <li>Department of Forest</li> <li>Department of Plant Resources</li> </ul>  | Permission and verification for Export                     |
|    |                         | <ul style="list-style-type: none"> <li>Forest Act 1993</li> <li>Forest Regulation, 1995</li> <li>Community Forestry Directive, 1996</li> <li>Inventory Guideline of Community Forestry, 2004</li> </ul> | <ul style="list-style-type: none"> <li>District Forest Office</li> <li>Chick post of DFO</li> <li>Community Forestry Users Groups (FCUGs)</li> </ul> | Permit for collection and release order for transportation |
|    |                         | <ul style="list-style-type: none"> <li>Buffer Zone Regulation, 1996</li> </ul>  | <ul style="list-style-type: none"> <li>Warden of concerned National parks or Reserves</li> </ul>   | Same as above  |
|    |                         | <ul style="list-style-type: none"> <li>Environmental Protection Act 1997</li> <li>Environmental Protection Regulation, 1997</li> </ul>  | <ul style="list-style-type: none"> <li>Department of Forest</li> </ul>   | Approval of IEE  |
|    |                         |   | <ul style="list-style-type: none"> <li>Ministry of Environment (for EIA)</li> </ul>  | Approval of EIA  |
|    |                         | <ul style="list-style-type: none"> <li>Local Self-governance Act 1999</li> <li>Local Self-Governance Regulation, 1999</li> </ul>  | <ul style="list-style-type: none"> <li>District Development Committee, Municipality, Village Development Committee</li> </ul>                        | Collection of local tax as per decision of council meeting |
| 3. | Processing              | <ul style="list-style-type: none"> <li>Environmental Protection Act 1997</li> <li>Environmental Protection Regulation, 1997</li> </ul>  | <ul style="list-style-type: none"> <li>Chief District Office</li> </ul>  | Pollution control  |
|    |                         | <ul style="list-style-type: none"> <li>Food Regulation, 1970</li> </ul>   | <ul style="list-style-type: none"> <li>Technology and Quality Control</li> </ul>   |  |
|    |                         | <ul style="list-style-type: none"> <li>Food Act, 1966</li> </ul>  | <ul style="list-style-type: none"> <li>Department of Food</li> </ul>   | Quality  |

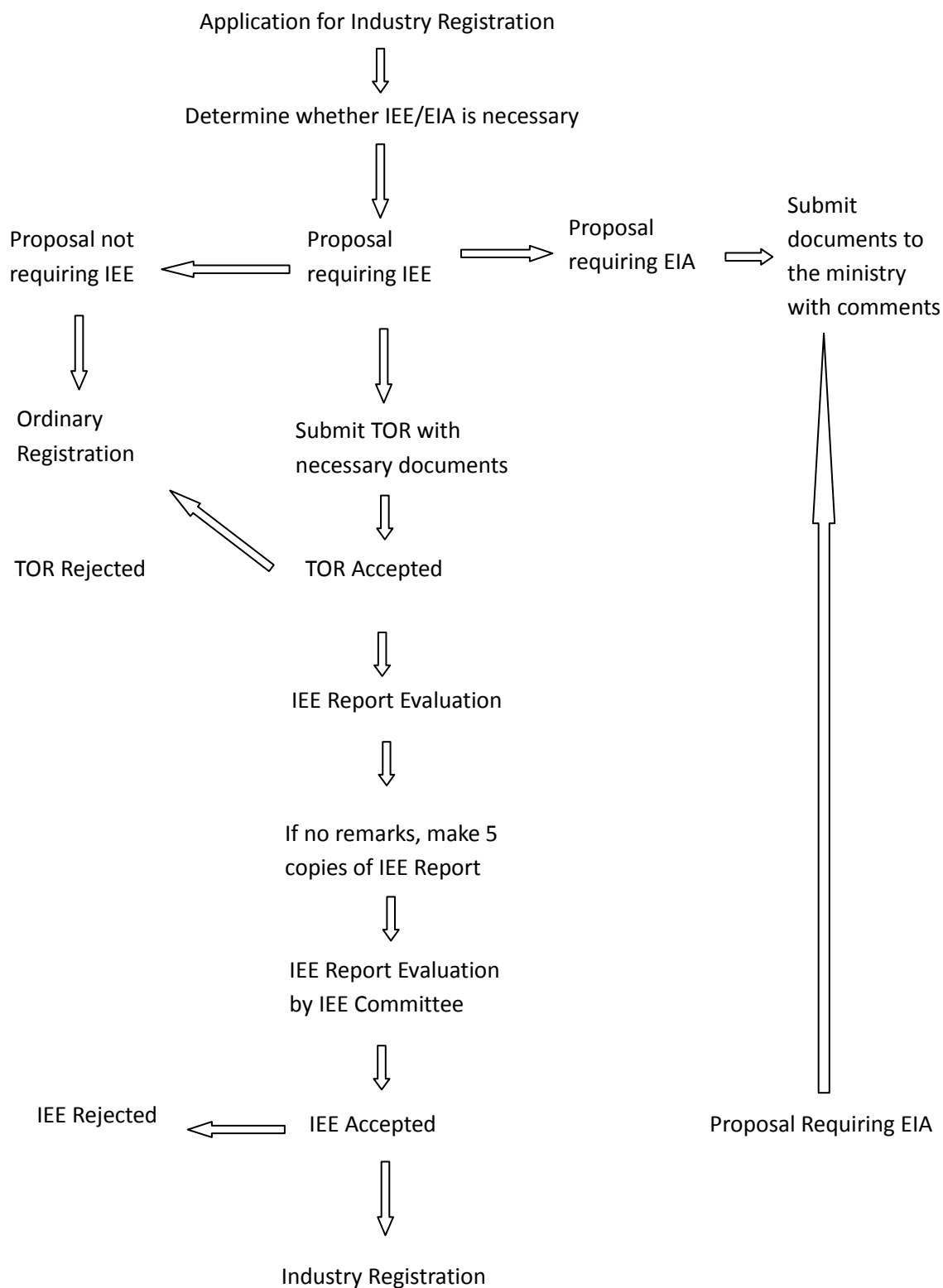
|    |   |  |   |  |
|----|---|--|---|--|
|    |   |  |   | control  |
|    |   | <ul style="list-style-type: none"> <li>• Consumer Rights Protection Act, 1997</li> </ul>   | <ul style="list-style-type: none"> <li>• District level monitoring unit</li> <li>• Chief District Office</li> </ul> | Quality assurance                                    |
|    |   | <ul style="list-style-type: none"> <li>• Nepal Standards Act 1980</li> <li>• Nepal Standards Regulation, 1984</li> </ul>   | <ul style="list-style-type: none"> <li>• Department of Nepal Standards and Measurement</li> </ul>                   | Maintain of standards                                |
|    |   | <ul style="list-style-type: none"> <li>• Medicine Act, 1979</li> </ul>   | <ul style="list-style-type: none"> <li>• Department of Drug</li> </ul>  | Quality control                                      |
| 4. | EIA/IEE (Environmental Standards)                                       | <ul style="list-style-type: none"> <li>• Environmental Protection Act 1997</li> <li>• Environmental Protection Regulation, 1997</li> </ul>   | <ul style="list-style-type: none"> <li>• Department of Forest</li> </ul>  | Approval of IEE                                      |
|    |   |  | <ul style="list-style-type: none"> <li>• Ministry of Environment (for EIA)</li> </ul>                               | Approval of EIA                                      |
|    |   |  | <ul style="list-style-type: none"> <li>• Chief District office</li> </ul>   | For monitoring and law enforcement                   |
| 5. | Enterprise Financing (Bank Loan, Insurance, Micro-finance)              | <ul style="list-style-type: none"> <li>• Bank and Financing Act, 2007</li> </ul>   | <ul style="list-style-type: none"> <li>• Bank and Financing institutions</li> </ul>                                 | Provide loan for enterprise                          |
|    |   | <ul style="list-style-type: none"> <li>• Financing Mediator Institution (Micro Financing) Act, 1998</li> </ul>   | <ul style="list-style-type: none"> <li>Micro Finance institutions</li> </ul>  | Provide loan for enterprise                          |
|    |   | <ul style="list-style-type: none"> <li>• Cooperative Act, 1992</li> </ul>  | <ul style="list-style-type: none"> <li>Cooperatives</li> </ul>  | Provide loan for enterprise                          |
|    |   | <ul style="list-style-type: none"> <li>• Insurance Act, 1993</li> </ul>  | <ul style="list-style-type: none"> <li>Insurance Companies</li> </ul>   | Provide insurance service                            |
| 6. | Taxes (VAT, Income Tax, local tax), service charge and registration fee | <ul style="list-style-type: none"> <li>• Income tax Act, 1992</li> <li>• Value Added Tax (VAT) Act, 1995</li> <li>• Local Self-Governance Regulation, 1999</li> <li>• Concerned laws as above mentioned in registration</li> </ul> | <ul style="list-style-type: none"> <li>• Department of Internal Revenue</li> <li>• Local Governments</li> </ul>     | Tax collection or tax exemption                      |
| 7. | Transportation (domestic)   | <ul style="list-style-type: none"> <li>• Forest Act, 1993</li> <li>• Forest Regulation</li> </ul>  | <ul style="list-style-type: none"> <li>• District Forest Office</li> <li>• Check post under DFO</li> </ul>          | Control of illegal transportation of forest products |
|    |   | <ul style="list-style-type: none"> <li>• Income Tax Act, 1992</li> </ul>   | <ul style="list-style-type: none"> <li>• DDC</li> </ul>   | Local tax collection                                 |
|    |   | <ul style="list-style-type: none"> <li>• Narcotic Drug (control) Act, 1977</li> </ul>  | <ul style="list-style-type: none"> <li>• Police/security related offices</li> </ul>                                 | Control of illegal trade                             |
|    |   | <ul style="list-style-type: none"> <li>• Income Tax Act, 1992</li> </ul>   | <ul style="list-style-type: none"> <li>• Department of Internal Revenue</li> </ul>                                  | Tax regulation                                       |
| 8. | Intellectual property   | <ul style="list-style-type: none"> <li>• Patent, design and trade mark Act, 1966</li> </ul>  | <ul style="list-style-type: none"> <li>• Department of industry</li> </ul>  | Registration of Patent, design                       |

|    |                              |   |  |  |
|----|------------------------------|---|--|--|
|    | (patenting,<br>trade mark)   |   |  | and trade mark                         |
| 9. | Marketing<br>(International) | <ul style="list-style-type: none"> <li>• Forest Act, 1993</li> <li>• CITES, 1973</li> </ul>                   | <ul style="list-style-type: none"> <li>• Department of Forest</li> <li>• Department of Plant Re-sources</li> </ul> | Permission and verification for Export |
|    |                              | <ul style="list-style-type: none"> <li>• Laws of WTO and bilateral or regional agreements on trade</li> </ul> | FNCCI  | Issue of certificate of origin         |
|    |                              | <ul style="list-style-type: none"> <li>• Plant protection Act, 2008</li> </ul>                                | Quarantine Offices under Department of Agriculture   | Issue of Quarantine certificate        |



## Annex – 2

### Steps of registering a forest-based enterprise



## Annex-3

### List of Documents for Industry Registration

| Registration    |                                     | Documents   |
|-----------------|-------------------------------------|---|
| Private firm    | Private firm registration Act, 1958 | <ul style="list-style-type: none"> <li>• Application as per Annex-6 (Guideline, 2009)</li> <li>• Certified copy of citizenship</li> <li>• Permission (only for industries requiring permission)</li> <li>• Skim (only for industries requiring permission and IEE/EIA)</li> <li>• Distance certified from the distance certification team</li> <li>• Recommendation from DFO with their comments</li> <li>• Sarjamin Muchulka</li> <li>• Land title (Lalpurja), with receipt of tax payment,</li> <li>• Acceptance letter from the neighbors, map and Manjurnama</li> <li>• Agreement of land/building taken in lease</li> <li>• Passport size photo- 2 copies</li> <li>• Application fee Rs 100.00 with ticket worth Rs. 5.00</li> <li>• Registration Fee</li> </ul>                 |
|                 | Joint Venture (Sajhedari) Act       | <ul style="list-style-type: none"> <li>• Application as per Annex-6 (Guideline, 2009)</li> <li>• Certified copy of citizenship of the members</li> <li>• Agreement amongst the members</li> <li>• Permission (only for industries requiring permission)</li> <li>• Skim (only for industries requiring permission and IEE/EIA)</li> <li>• Distance certified from the distance certification team</li> <li>• Recommendation from DFO with their comments</li> <li>• <i>Sarjamin Muchulka</i></li> <li>• Land title (Lalpurja), with receipt of tax payment,</li> <li>• Acceptance letter from the neighbors, map and Manjurnama</li> <li>• Agreement of land/building taken in lease</li> <li>• Passport size photo of members- 2/2 copies</li> <li>• Application fee Rs 5</li> </ul> |
| Private Limited | Private Limited or Public Limited   | <ul style="list-style-type: none"> <li>• Application as per Annex-6 (Guideline, 2009)</li> <li>• Certified copy of citizenship of founder shareholders.</li> <li>• Company registration certificate</li> <li>• Permission (only for industries requiring permission)</li> <li>• Skim (only for industries requiring permission and IEE/EIA)</li> <li>• Distance certified from the distance certification team</li> <li>• Recommendation from DFO with their comments</li> <li>• Sarjamin Muchulka</li> <li>• Land title (Lalpurja), with receipt of tax payment,</li> <li>• Acceptance letter from the neighbors, map and Manjurnama</li> <li>• Agreement of land/building taken in lease</li> <li>• Passport size photo- 2/2 copies</li> <li>• Application fee Rs. 5.00</li> </ul>  |

## Annex-4

### Conditions that the enterprises should follow

#### 1. Forest Based Industries

- A. For the forest based industries, as per the letter of Ministry of Forests and Soil conservation dated 2064/1/10, the provisions given below should be followed during registration.
- When the raw materials are to be supplied from forest area, enterprises should get pre-approval from the Ministry of Forests and Soil Conservation.
  - When the raw materials are not to be supplied from the forest area, enterprises should show the source of the raw materials, details about raw materials supply, and the authority should be convinced.
  - The enterprises must be established 2 KM away from the forests (including conservation area and buffer zone) in Terai and 1 KM away from the forests (including conservation area and buffer zone) in areas other than Terai.
  - For the Community Forests, the distance obligation will not apply provided they comply with Forest Regulation Rule 32 (4). *Rule 32(4) says “In case the Users' Group is capable of running an industry based on forest products according to the work plan, it may run such industry outside the area of the Community Forest after obtaining the approval of concerned agency on the recommendation of the District Forest Officer.* But according to Environment Protection Regulation 2054, the brick, tile and saw mills cannot be established within 5KM distance from the forest area.
  - The industries like saw mills, brick, tile etc already established within 2KM in Terai and 1KM in other areas must be shifted beyond the 2KM and 3KM respectively. The license will be made available from Ministry of Commerce and Supply and the ministry must always provide the information of such license.
  - While shifting ownership (Namsari), no need to get acceptance from the ministry of forests and soil conservation but such information should be given to the forest offices.
- B. The forest based small industries do not need the distance approval provided that they consume less than 100 cubic feet timber per year, get timber by themselves or from contractor and have taken permission to establish the industry in district headquarter. (letter of Ministry of Forests and Soil conservation dated 2053/3/7)
- C. The distance limit (2KM in Terai and 1KM in other areas) will not apply when industries are to be established in industrial estates. (Decision# 154 of Industrial Promotion Board dated 2057/2/26)
- D. The distance limit (2KM in Terai and 1KM in hills) will not apply when forest based furniture industries are to be established in areas of Kathmandu valley (for other districts of Kathmandu valley- municipalities and district headquarters. (Decision# 154 of Industrial Promotion Board dated 2057/6/13)

## **2. Furniture, Saw Mill and Katha Industries**

- To register the forest based furniture, saw mill and Katha mill should submit the recommendations of the concerned VDC or municipality along with the approval of the neighbors (Sadhiyar) and Sarjimin Muchulka saying no-pollution.
- The furniture industries will get permission to establish and use band saw of 36 inch at most in areas of Kathmandu valley other than the municipalities. For other areas, such industries will get permission of using 36 inches band saw after looking at the appropriateness. When the industries already registered and use band saw of more than 36 inches apply, they have to show the approval of the neighbors (Sadhiyar Muchulka), recommendation of VDC/municipality. Then they will get permission to use up to 36 inch single band saw provided they will comply the following conditions
  - No logs will be sawn
  - No trolleys will be used and
  - Only the timber for the own industry will be sawn. No other timber will be sawn

## **3. NTFPs, Lokta and Other Forest Based Industries**

- The industries that process NTFPs or use Lokta as raw materials should get approval from the concerned District Forest Office before their registration.
- The team comprised of the officer representative of District Forest Office (coordinator), Amin of Napi Office (member) and representative of District Cottage and Small Industries (member) will certify the distance between forest boundary and the industry. (Letter of Department of Forest, Forest Product Section dated 2059/7/15).

### **Conditions that should be articulated during Industries Registration**

Apart from the conditions apply according to the type and nature of the industries, the following terms and conditions should always be articulated during the registration of all types of industries.

- The existing and upcoming rules and regulations will be followed during industry operation
- Appropriate pollution reduction measures should be managed.
- No disturbances to the neighbors during industries operation.
- No permission to go against Customer Protection Act/Regulation
- The inner industries operation should not be visible from the main road. This provision will be adjusted according to the nature of the industries.
- The industrial wastage and by-products will be managed appropriately.
- In case the industry name duplication, the industries registered on later date should amend their name.
- While giving permission or getting registration of the industries requiring IEE/EIA, the terms of conditions of IEE/EIA should be written in the license and registration certificate.

## **Annex-5**

### **Facilities to Cottage and Small Industries as per Industrial Enterprise Act, 2049**

- Cottage industries do not have to pay income tax, sales tax and excise duty.
- Agriculture and forest based industries other than saw mills and Katha will get income tax exemption for 5 years and additional 2 years income tax exemption if they consume 90 percent or more than 90 percent raw materials from the country.
- Industries (other than tobacco, alcohol, beer) established in remote, undeveloped, underdeveloped and ordinary developed areas will get income tax discount by 60, 50, 20 and 10 percent and excise tax discount by 35, 25, 15, and 10 percent discount respectively.
- Forest-based industry may be made available any forest on a leasehold basis.

### **Procedure for claiming the facilities**

- The cottage and small industries should apply to the Cottage and Small Industries Development Board for the facilities specified in the Industrial Enterprise Act. The board then will certify the documents received and submit to the department with its comments on whether such the industries should get the demanded facilities. For this the Cottage and Small Industries Development Board should write the details (of Annex 24 of Guideline) to the department.
- Department will submit the document (proposal), then, One Window Committee formed under Industrial Enterprise Act, 2049 (17) decides whether such facilities are to be granted. Only after such decision, the department will correspond to the concerned office for implementation.
- Department will certify (that the industries are eligible to get the facilities) and inform the inland revenue office in writing that the industries deserve discount of income tax, sales tax and excise duty.