

Implications of the New Cooperative Act on the Financial Sector in Nepal

Definition

A cooperative (also known as co-operative, co-op, or coop) is "an autonomous association of persons united voluntarily to meet their common economic, social, and cultural needs and aspirations through a jointly-owned and democratically-controlled enterprise¹". Cooperatives may include:

- non-profit community organizations
- businesses owned and managed by the people who use their services (a consumer cooperative)
- organisations managed by the people who work there (worker cooperatives)
- organisations managed by the people to whom they provide accommodation (housing cooperatives)
- hybrids such as worker cooperatives that are also consumer cooperatives or credit unions
- multi-stakeholder cooperatives such as those that bring together civil society and local actors to deliver community needs
- second and third-tier cooperatives whose members are other cooperatives

New Cooperative Act 2017 – Highlights and Implications for the Cooperative Sector in Nepal

After 26 years, the Cooperative Act of 1991 has been revised and endorsed on October 18, 2017. During this period, the Nepalese Cooperative sector grew at an exponential magnitude. In 1990 (when the Act was last revised); there were 830 cooperative societies and 30+ district unions. As on July 2016, there were 33,599 cooperatives followed by numerous different types of district unions and 22 central unions. Hence, it was obvious that the old act needed to be updated and replaced by a new robust act that would enable better regulations and delivery of financial services. The highlights of the new Cooperative Act are:

- i. Comprehensive in nature (20 Chapters, 152 clauses versus 12 chapters and 49 clauses in the previous act)
- ii. A separate chapter has been added for Savings and Credit Operations
- iii. A separate chapter for Cooperative Banks has been added
- iv. Creation of Cooperative Development Fund
- v. Provision made for creating a Loan Collection Jurisdictional Authority (Nyayadhikaran)
- vi. Gender friendly (in comparison to the earlier Act)– advocates for women representation in the Board
- vii. Huge penalties built in to ensure safety of members' savings
- viii. Takes new federal structure into accounts

¹ Wikipedia

The implications of the new Act on the Cooperative sector in Nepal are listed below:

S. No.	New Cooperative Act 2017	Implications for the Cooperative sector
1.	<p>After 26 years, the Cooperative Act of 1991 has been revised and endorsed. Given the changes, and the exponential growth during the time; it was obvious that the old act needed to be replaced by a new robust act.</p>	<ul style="list-style-type: none"> • Savings and Credit Cooperatives have been advocating for a separate Credit Union Act. The new Act has a separate chapter on this; and if the capacity of the cooperative department to monitor cooperatives is increased, it will help regulate the sector. • Implications: Cooperatives supported by various financial inclusion development initiatives may have to start reducing their non-savings and credit activities and focus on financial services.
2.	<p>Selected specific provisions of the new Act:</p> <ul style="list-style-type: none"> • Minimum numbers of members for registration increased • Minimum number of society to form district unions increased • Numbers defined according to the geographical context (remote-less, accessible- high) • Provision for specialized cooperatives (professional cooperatives without the right to be elected in union or federation) • Restriction for forming more than one union for similar purpose 	<ul style="list-style-type: none"> • This will help consolidate the growth of members and meet the scale of operations for cooperatives, thereby making it easier for them to qualify for investments from microfinance institutions.

S. No.	New Cooperative Act 2017	Implications for the Cooperative sector
3	<ul style="list-style-type: none"> Clarify on the role of NRB in registering Cooperative Banks Area of operation defined (provision for increasing or reducing work areas) Provision for running projects by cooperatives By-law amendment simple majority previously 2/3rd Membership provision for non-individuals Restriction for becoming a member in two or more cooperatives Restriction for board members to be employee 	<ul style="list-style-type: none"> The clarity between NRB's and Cooperative Department's roles are expected to reduce ambiguity around monitoring, regulatory and other functions. The governance control mechanisms introduced around limiting memberships etc. would lead to a decrease in ever-greening of loans, and creation of a poverty debt trap especially for first time borrowers with limited financial literacy.
4	<ul style="list-style-type: none"> Conflict of interest for Board Members defined Provision for minimum female representation in the Board Authority for Registrar to appoint ad-hoc board Need to consult Nepal Rastra Bank for dissolution of Board Duties and rights of Accounts Committee explained 	<ul style="list-style-type: none"> The new act has made a conscious decision to include women at the decision-making level (Board Members). Given that a majority of cooperative members are women, this was a much-needed improvement. The new Act has also put mechanisms in place for regulating Cooperatives to avert situations where the Board has been dissolved to avert responsibilities for misusing and loss of deposits.
5	<ul style="list-style-type: none"> Restriction for non-SACCOS to undertake savings and credit activities Interest rate "spread" defined in the act (i.e. 6%) Provision for defining reference interest rate Savings mobilization up to 15 times of equity Share amount specified at NPR 100 Provisions for reserve funds and special reserves defined (new provision for fixing percentage in patronage refund defined at 25%) 	<ul style="list-style-type: none"> Ideally, the provision such as defining the interest rate spread could have ideally been left for the Cooperative Rule that will follow the Act or to the Cooperative directives and standards. Unfortunately, what this means is that if there were to be a change in the interest spread rates, the Act will have to be endorsed by the parliament. This is likely to cause more delays. Increase in provisioning and limitation in dividend distribution will ensure responsibility, ownership and eventually a good financial health for the institutions.

S. No.	New Cooperative Act 2017	Implications for the Cooperative sector
	<ul style="list-style-type: none"> • Mandatory provision for "Cooperative Promotion Fund" defined 0.5 % (operational modality defined) • Dividend distribution limited to 18% 	
6	<ul style="list-style-type: none"> • Tax relief for specific geographical areas • Tax relief for reserve funds and patronage refund fund • Tax relief for specialized projects • Provision for undertaking "sick enterprises" by workers' Cooperatives • Debt collection through auctioning collaterals • Provision for Credit Information Bureau • Loan collection Jurisdictional Authority (Nyayadhikaran) • Inspection and supervision of coops and coop banks • Provision for investigation of cooperatives enabled by application from 5% members • Provision of inspection by Ministry of Cooperatives 	<ul style="list-style-type: none"> • The challenges of resolving the issues of previous "defaulting cooperatives" may be resolved, provided there is adequate resources to do so. • Meanwhile, the NRB's role is clarified and limited to supervising cooperative banks. • Although provisions for monitoring and recovery have been built into the Act, it is highly unlikely that these provisions will be implemented effectively unless there are adequate resources allotted to the responsible departments.
7	<ul style="list-style-type: none"> • Provision for Cooperative savings and loan guarantee fund • Provision for stabilization fund • A separate chapter for declaring problem cooperatives • Penalties increased significantly • Provision for social audit • Provision for Cooperative education at school and colleges • A separate chapter for Cooperative Banks added • Provision for taking over management of cooperative banks by NRB • Interim arrangement till federal law 	<ul style="list-style-type: none"> • The provisioning of Loan Guarantee Funds is proposed considering regional, global practices in credit union movement. • Increased penalties are expected to reduce and discourage frauds. • It is important to monitor how the federal structure will perform in relation to drawing their own laws; including regulation for cooperatives for their own federal entity.

Implication of Decentralization on the Cooperative Sector

In the context of decentralization from the government's perspective, the most complete forms of decentralization are privatization and deregulation because they shift responsibility for functions from the public to the private sector. Privatization and deregulation are usually, but not always, accompanied by economic liberalization and market development policies. They allow functions that had been primarily or exclusively the responsibility of government to be carried out by businesses, community groups, cooperatives, private voluntary associations, and other non-government institutions.

In recent years, Nepalese financial institutions - including those operating in remote, rural regions have been commercially motivated. At the same time, amongst the cooperatives that mostly operate in regions where regulated financial institutions are absent, there is little or no policies that regulates the lending. Thus, the lending relationships between rural financial institutions and their clients are more likely to continue to be driven by commercial purposes rather than central bank and or government policies.

Monitoring and Evaluation: Decentralization can lead to misaligned responsibilities because the process and criteria for monitoring and regulation of local cooperatives is incomplete, possibly for political reasons. Although there is a delegated responsibility for the Central Bank to oversee the financial sector reforms in the country, it may have a limited role and authority. While decentralization was in some cases intended to strengthen the political power of lower tiers of government vis - à - vis the center, it has also increased the possibility of political capture within these lower tiers. Often, "village heads" influence selection of members of the council that are elected to represent the nest interests of the local communities; and therefore, accountability to the villagers can be weak. This may affect the financial sector as it continues to receive development aid to pursue new, innovative financial products and services with an ambition of expanding financial outreach in the underserved regions.

Conclusion: The sector should continue to advocate for greater participation of the public and private sector. This has been enabled through investments in recent years large scale projects that have brought innovation and displayed sustainable business models while enhancing financial inclusion in Nepal. This has in turn helped achieve economic prosperity by creating income generating opportunities for the beneficiaries, and maximum utilization of available resources through leveraging private sector investments while offsetting some element of the risks to encourage participation beyond the usual geographic regions and demographics.