

PROBLEMS AND PROSPECTS OF LEASING BUSINESS IN NEPAL

A Thesis



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DECLARATION

I hereby declare that the work reported in this thesis entitled **Problem and Prospects of Leasing Business in Nepal**, submitted to Nepal Commerce Campus, Tribhuvan University is my original work. It is done in the form of partial fulfillment of the requirements for the **Master of Business Studies (M.B.S.)** under the supervision of **Prof. Dr. Bihari Binod Pokharel** and **Mr. Umesh Kumar Koirala**, Lecturer, Nepal Commerce Campus.

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LIST OF ABBREVIATIONS

AMT	=	Alternative Minimum Tax
ANOVA	=	Analysis of Variance
Co.	=	Company
IFC	=	International Finance Corporation
ILFC	=	International Leasing and Finance Co. Ltd.
IRR	=	Internal Rate Return
Ltd.	=	Limited
MBSL	=	Merchant Bank of Srilanka
NBL	=	Nepal Bank Limited
NSLMB	=	Nepal Sir Lanka Merchant Bank Ltd
NRB	=	Nepal Rastra Bank
UFCO	=	Union Finance Company
UK	=	United Kingdom
UN	=	United Nations
USA	=	United States of America
WMBFC	=	World Merchant Banking and Finance Company

CHAPTER- I

INTRODUCTION

1.1 Background of the Study

Development of any country is demonstrated by the development of the financial sector of the country. The Financial sector of any country comprises of Banks, co-operative societies, insurance companies, finance companies, stock markets, foreign exchange markets, mutual funds, provident funds etc. And stock exchanges via primary markets, banks & financial companies via short-term and other types loans are recognized as the main sources of much needed capital input for industries and Business

Finance is primary prerequisite in establishing and developing any business organization. Finance helps bringing together all the factors of production in industrial unit. Therefore financing is a critical element for success of business. In the absence of adequate finance, even the business having high potentiality may fail. Financial decisions impact on the long-range financial strategies of the firm thereby putting effect on the value of the firm.

The basic purpose of obtaining fund is to acquire assets. We do not acquire plant and equipment with the aim of reselling it at a profit. We really need only the service of those fixed assets. If we do not wish to have title to the assets. If it is just the service we seek. We should consider leasing the assets. Thus, leasing is the means of obtaining the services of fixed assets just as the sell of bonds is usually a means of acquiring both the services of and title to various assets. More specifically, Lease is a contractual arrangement whereby the owner of the property (lessor) allows another party (lessee) to use the service of the property for a specified period of time. The lesser retains title to the property. The contract calling for periodic rental payment is fixed and may not be cancelled for a definite period of time. Usually the lessee may continue to use the property after the initial period of the lease at a reduced rental specified

in the lease. Sometimes, he may also be given an option to purchase the property.

Leasing simultaneously provides for the use of assets and their financing, one way of obtaining their use is to buy them, but an alternative is to lease them. Virtually, any kind of fixed assets that can be purchased can be leased. In many cases, leasing can be a perfect substitute for borrowing. One advantage over debt is that the lessor has a better position than creditors if the user firm experiences financial difficulties. Since lease is a contract, both the parties should meet their obligations. If the lessee does not meet the lease obligation, the lessor has a stronger legal right to take back the assets, because the lessor still legally owns it. A creditor even a secured creditor encounters cost and delays in recovering assets that have been directly or indirectly financed. Since the lessor has less risk than other financing sources used in acquiring assets, the riskier the firm seeking financing the greater is the reason for the supplier of financing to formulate a leasing arrangement rather than a loan. The relative tax positions of lessor and users of assets may also affect the lease versus borrow decision.

The foundation for growth in leasing is

- I) Differences in the protection afforded the lessor and lender in the event of bankruptcy and
- II) Differences in the ability of companies, financial institutions, and individuals to take advantage of the tax benefits associated with owning of asset, of the two, tax differences have by far the greater influence. Companies that pay no or low taxes may be able to realize some of the tax benefits associated with depreciation via high tax bracketed lessor passing them off through lower lease payment.

Leasing has been well recognized in financing the project cost of new industrial enterprises, financing the expansion, modernization and diversification programs of the existing industrial units. Further, leasing could serve the ends of

enlivening. The sick industrial units thought indigenous as well as import leasing arrangement. For the full utilization of development strategy has proved its effectiveness and the government's role in this context should be to create favorable environment for the private sector investments, democracy, social justice and development. The least developed countries are in need of substantially large investment for development, particularly of the physical as well as social infrastructure. But such investment has been restricted due to low level of internal revenue mobilization in these countries. The developing countries, today, can neither ignore nor avoid the liberalization and globalizations his option of policy choice has been extremely limited particularly after the collapse of centrally planned economic system. At this moment liberalization and globalization has come to occupy a central stage all over the world.

History shows that Rail Car financing aided the growth of industrial revolution by providing Rail roads as means to expand their services of getting goods to and from market in western world and the United States in the last half of the 19th century. Similarly, in USA, from 1950s the development of airlines was done only through lease financing. In 1960s true lease came into vogue, which had stimulant on account of favorable tax laws.

Leasing companies can meet the requirement of finance for modernization, expansion or diversification for industrial sector as an alternative source of finance rather than depending fully upon help of financial institutions. Theoretically almost all the assets can be leased. Lease contract may be for short-term or long-term and every type of leasing has their own specialty in the business sector. Properties like plant, equipments and real estate etc are leased for long period of time.

Lease financing is an activity of non-banking type. Leasing companies are therefore non-banking financial institutions, which acts as financing intermediaries in the economy. These non-banking financial institutions

(NBFI) derive importance for providing convenience for the savers and borrowers in their capacity as repositories of savings and lending institutions. They do not accept deposit but compete with banks in time deposit. It is also a merchant banking activity, which has been included in the operational scope of merchant banks, which acts as financial intermediaries offering various services to be business world including lease finance as their fund based activity.

Leasing could be advantageous to society if its social benefits outweigh the loss in taxes. Shortage of investable funds constrains investment and therefore production. Leasing companies encourage investment by making funds available in a less cumbersome and speedy way; On the other hand lease financing is a real gap filler for non-priority and small-scale sector. Therefore, the objectives of government, banks and financial institutions should be to create policy and market conditions so that the leasing activity contributes to economic growth and financial efficiency.

1.2 Profile of the Organization Selected

International Leasing & Finance Co. Ltd. (ILFC), an emerging symbol in a combination of quality, reliability & professionalism, stands with its unique pride for being the key role player in introducing leasing business in Nepal. With the prime objective to provide the people of the nation with creative financing alternatives of international standards, ILFC evolved as a brainchild of the Nepalese & Korean counterparts after the constant mutual efforts over the years.

Established on December 11, 1992 under the public company legislation of the kingdom of Nepal, ILFC obtained business-operating license from the central bank of Nepal on September 18, 1995 and started its operations from October 31, 1995. Since then it has been continuously rendering variety of financial services according to the aspirations of the Nepalese people.

VISION

The perpetuity of its existence is for the superiority of lives of our valued clients, and combining the quality, reliability & professionalism with the customers' welfare has been only business challenge for it.

Foreign partners

KDB capital corporation (KDB capital), the largest leasing company in the republic of Korea and one among the top 3 largest Leasing companies within the Asian continent, has been participating in the management of ILFC providing all the technical know how as a foreign partner since the very inception of the company.

International Finance Corporation (IFC), a subsidiary of World Bank Group & renowned financial Institutions in the world, has an equity participation in ILFC. This corporate tie-up of ILFC with IFC has enabled us to stand as one of the Multinational Financial Institutions in Nepal

1.3 Focus of the Study

Without proper and timely reformation, financial sector annoy take full speeded on ties development process's Nepal has adopted open, liberal and market oriented economic policy since late 1980s and simultaneously financial sector reform programmes have been initiated. But with the passage of time, financial sector is becoming more exciting, challenging and ever-changing sector due to increased economic liberalization and globalization.

To cope with such complex situating, financial innovation should be given priority so that sophisticated financial market, improved financial instruments as well as efficient and effective financial process can be developed. Presently there is proliferation of various banking and non banking financial institutions in the country offering wide range of services including many new type of

financial services like venture capital, leasing, merchant banking, mutual fund etc.

Among such new financial services leasing is one of the innovative financial service, which carry extremely different philosophical idea about the use of capital asset in productive activates. Leasing concept advocate that the important thing is the service war get from using asset, not the ownership on it. Therefore, it sis wise to take serve of any asset on rental basis without purchasing it. After the World War II, leasing has achieved significant growth in a global perspective. In Nepal also, it has been started, but people have not been well informed about this financial service. There are number of ambiguities about it. Its real financial meaning has not yet been realized in Nepalese financial community. It is, therefore this research is focused on the study of lease financing in the context of Nepal.

1.4 Statement of the Problem

The problem towards which this study is directed is to explore and highlight about equipment leasing business in Nepal

In an international scenario, industrialized countries like America, Japan, United Kingdom, Italy, Germany, France etc have been carrying very large volume of business successfully through leasing. It has remained in the first priority for financing the capital asset requirement in these countries. After the World War II, when the development infrastructure was destroyed and economy was undercapitalized, leasing was used as the most effective tool to rebuild the country. Since then, leasing has been playing significant role in the industrialization process of these countries. There is no limitation to take any asset on lease. Therefore, leasing in these countries covers wide varieties of assts i.e. moveable, immovable, small, large etc. public and private sector both have put effort for the development of leasing business. Leasing has been accepted as the most effective tool for mobilizing available resources in the

productive sector. Laws are made favorable so as to encourage the leasing business. Especially, tax law provides tax concession from which both lesser and lessee are benefited. Further, government has remained always supportive to the business. In these countries, huge invest mint tax credit allowance is provided to promote this business. Almost all types of financial institution are legally allowed to carry leasing business. Moreover, manufacturing companies are performing leasing business as an effective marketing device for their products.

In a like manner, leasing has proved its beneficiary in many developing countries also like Brazil, India, Taiwan, Korea, Silence, Bangladesh etc. it has been established as a growing industry in these countries. In such developing economics, leasing business is getting more rapid development because of its effective ensues in supporting small-scale industries instead of large industrial establishments. As a result leasing has achieved remarkable success in many such countries. The success of Korean leasing business can be cited as an example where during the period of 3 years (1976-1979) the lease volume increased from \$8.9 billion to \$ 98.8 billion.

This situation of Nepalese leasing business has created serious need to conduct research, which can explore and highlight the real picture of leasing business in Nepal. Therefore, this research is being motivated and directed towards following research problems:

-) What is the important information about equipment leasing business of Nepal that need to be highlighted?
-) What are the legal provisions available in leasing business?
-) How the leasing is being practicing in Nepal?
-) How the finance companies are viewing to the matters relating to the leasing business of Nepal?

1.5. Objective of Study

The main objective of this study is to study the growth of leasing business in Nepal. To attain the main objective, following other specific objectives have been set up:

-) To study and analyze the introduction growth and development of leasing business in Nepal.
-) To find about the lease rental calculation method used by the lessor/finance company and to study the schedule of payment of the lease rental.
-) To find the problems and future prospect related to leasing business in Nepal.
-) To study and examine the existing legal provisions relating to the leasing business in Nepal.

1.6 Significance of the Study

In this world of the financial market leasing has also been one of the very good areas of investment. The world today is making steady progress in leasing business. United States of America has the largest leasing business in the world. It has been significantly influenced by the tax policy, particularly ever since Economy Recovery Tax Act was adopted in 1981 giving lessor and lessee new stage for negotiation. The outstanding growth of leasing business in USA was due to treatment of leasing by ACT and the new 'safe harbor' leasing rules adopted by the United States Tax authorities. It is called 'safe harbor' because leased structure will not be challenged within their guidelines. Other developed countries like Germany, France, United Kingdom and Japan also has fast growing leasing businesses.

In Nepal leasing business is in its infancy stage. Many finance companies have established intending to perform leasing business. Out of them many companies have not even yet started that business. Among the 54 non-bank

financial companies only 4 of them are performing leasing business. Among them 3 are from the Kathmandu valley and one from the Hetauda. To name them they are:

1. Union Finance Company (UFCO)
2. International Leasing and Finance Company (ILFC)
3. Nepal Sir Lanka Merchant Bank Ltd (NSLMB)
4. World Merchant Banking and Finance Company (WMBFC)

Even though they are doing many leasing business, these companies are not making as much profit as they could. There could have been more profit if we have proper tax rates and depreciation charges. They are making only accounting profit which if one sees from financial point of view one can clearly find that has been as much profit as it has been calculated. These amounts of the lower profit can be obtained if we use factors like future value of money and opportunity lost. So this study will try to find out the problems related with the leasing business in Nepal. It will also try to find the solutions for the problems found. Therefore the effort is made to highlight the significance of the study, which are as follows:

- It will help enhancing awareness about leasing business in Nepal
- This study will try to show the scenarios of current leasing business situation in Nepal or say it will portray the picture of leasing business. Therefore it will hold practical value to concerned institution, policy makers and regulatory body.
- Since many people are unaware of benefits of leasing business, it will also be helpful for them to choose for the better alternative between loan and lease.
- It will fulfill the research gap in the leasing business sector of Nepal.
- The promising result of this research also may help to encourage the other business house to invest more on leasing business in coming future.

1.7 Limitations of the Study

The Study has the following limitations:

-) The accuracy of the information is the main ingredient for the success of this research. If this information is not true, whole findings of the study will be meaning less.
-) This study is constrained only to financial lease excluding the short term operating lease.
-) This study covers only those finance companies, which have been located at Kathmandu valley.
-) The Study is more focused on lessor's point of view.

1.8 Organization of the Study

The study will be organized into five chapters:

Chapter I: Introduction

The chapter 1 deals with subject matter of the study consisting background of the study, profile of the organization, statement of the problem, objective of the study, significance of the study, research methodology, limitation of the study, review of related studies and organization of the study.

Chapter II: Review of Literature

The chapter 2, deals with the theoretical review of studies review of previous study and justification of the study.

Chapter III: Research Methodology

The chapter 3 contains the information regarding the methodologies employed to attain the objective of the study.

Chapter IV: Presentation and Analysis of Data

The chapter 4 contains the presentation and analysis of the data collected during the whole survey period and its major findings.

Chapter V: Summary, Conclusion and Recommendation

The chapter 5 contains the summary of the findings of the survey and its conclusion and recommendation to the finance/ leasing company.

CHAPTER - II

REVIEW OF LITERATURE

This chapter has been especially designed to achieve the concept of leasing business. This chapter highlights the relating to present study of lease and leasing business in Nepal and other different countries. It will help the reader of this thesis to better understand the lease and its aspects before knowing about its problems and prospects. For this purpose, the study has covered theoretical or conceptual review as well as the review of other relevant researches regarding leasing business available in Nepal.

2.1 Conceptual Review

As far as the theoretical or conceptual aspect of leasing business is concerned, the study has aimed at making it comprehensive. Therefore, under this topic, various aspects of leasing business have been studied like meaning and definition of lease, basic elements of lease, types of lease, types of asset that can be leased, advantage of lease to the leaser, advantage of lease to the lessee, limitation of leasing, tax consideration in leasing, sources of value in leasing, accounting for leasing, evaluation of lease by lessor, things to be considered while leasing, origin of concept of leasing, growth of leasing in developed nations and developing nations, fundamentals of leasing business, important aspects of leasing business etc.

2.1.1 Meaning of Leasing

Leasing is a contract or an agreement in which one party (the owner or the lessor) conveys to another party (the user of the lessee) the exclusive right to use an asset in exchange for a series of payment (the lease rent) for a specific period of time. It, therefore, embraces an interest rate cost to the lessee and an interest rate to the lessor.

When a lease is terminated, the leased equipment reverts back to the lessor unless there is option to purchase the equipment or take out a new lease (Brealey & Mayers, 1991:654). The lessee may continue to use the property after the initial period of the lease at a reduced rental specified in the lease. The lessor in a lease arrangement is the party that has the title to the property leased and the lessee is the party that has the possession and use of the asset being leased (Rao, 1991:797).

conceptually, a lease may be defined as a contractual arrangement/ transaction in which a party owning as assets/ equipment (lessor) provides the assets for use to another/ transfer the right to use equipment to the user (lessee) over a certain/ for an agreed period of the time for consideration in the form of / in return for periodic payment (rentals) with or without a further payment, premium. (Khan & Jain, 1999: 9.1)

Leasing is a contract or an agreement in which one party (the owner or the lessor) conveys to another party (the user or the lessee) the exclusive right to use an asset in exchange for a series of payment (the rent) for a specific period of time. It, therefore, embraces an interest rate cost to the lessee and an interest rate return to the lessor.

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Leasing is a source of intermediated and long term financing. Leasing is a method of acquiring the right to use the assets for a specified period of time without obtaining ownership or title. A lease is a contract whereby the owner of

an asset (the lessor) grants to another party (the lessee) the exclusive right to use the asset, usually for an agreed period of time, in return for the payment of the rent. Most of us are familiar with leases of houses, apartments, offices, or telephones. Leasing has been an important part in business in recent decades, like leasing of business assets such as cars and trucks, computers of equipment and manufacturing plants. This has been growing business for owner of the certain asset as most of the new business firms do not possess enough capital to own an asset or rather they find it beneficial to lease than to purchase. So, the business firms usually leases the assets and uses it in their business without having to buy it. For this advantage, the lessee incurs several obligations. First and foremost is the obligation to make periodic lease payments, usually monthly or quarterly and in advance. Also, the lease contract specifies who is to maintenance, repairs, taxes and insurance. Under a net lease, the lessee pays these costs.

The lease contract typically specifies some kind of option to the lessee at expiration. It may involve renewal, where the lessee has thr right to renew the lessee for another period, either at the same rent or at a different, usually lower rent. the option might be to purchase the asset at expiration. for tax reasons, the purchase price must not be significantly lower than fair market value. if the lessee dose not exercise its option, the lessor takes possession of the assets and is entitled to any residual value associated with it.

Because of the contractual nature of a financial lease obligation, it must be regarded as a form of financing. it is used in place of other methods of financing to acquire the use of an asset. An alternative method of financing might be to purchase the assets and finance its acquisition with debt. Both the obligation must be met. Inability to meet these obligations will result in financial embarrassment.

2.1.2 Basic Elements of Lease

The essential elements of leasing are the following:

) Parties to the contract

There are essentially two parties to a contract of lease financing. They are the owner and the user respectively called the lessor and the lessee. Lessor as well as lessees may be individuals, partnerships, joint stock companies, and corporations or financial institutions. Sometimes, there may be joint lessor and joint lessee particularly where the properties or the amount of finance involved is enormous. Besides, there may be a lease broker who acts as an intermediary in arranging lease deals. They charge certain percentage of fees for their services. Lease contract may involve a lease financier, who refinances the lessor either by providing term loan or by subscribing to equity under a specific refinance scheme.

) Asset

The asset, property or equipment to be leased is the subject matter of a lease contract. The asset may be an automobile, plant and machinery, equipment, land and building, factory, a running business, aircraft and so on. The asset must, however, be of lessees' choice suitable for his business needs.

) Ownership separated from user

The essence of lease financing contract is that during the lease tenure, ownership of the asset vests with the lessor and its use is allowed to the lessee. On the expiry of the lease tenure the asset reverts to the lessor.

) Lease rental

The consideration, which the lessee pays to the lessor for the lease transaction, is the lease rental. The lease rentals are so structured as to compensate the

lessor for the investment made in the asset, the interest made on the investment, repairs, insurance if any borne by the lessor, and servicing charge over the lease period.

J **Term of lease**

The term of lease is the period for which the arrangement of lease remains in operation. Every lease should have a definite period, otherwise it will be legally inoperative, and the lease period sometimes may stretch over the entire economic life of the asset (i.e. finance lease) or a period shorter than the useful life of the asset (i.e. operating lease), the lease may be perpetual that is, with an option at the end of lease period to renew the lease for a further specific period.

J **Modes of Termination of Lease**

At the end of the lease period, the lease is terminated and there are various courses possible for this purpose:

- a) The lease is renewed on a perpetual basis or for a definite period, or
- b) The asset reverts to the lessor, or
- c) The asset reverts to the lessor sells it to a third party, or
- d) The lessor sells the asset to the lessee.

The parties may mutually agree to and choose any of the aforesaid alternatives at the beginning of the lease contract. (Khan & Jain, 1999: 9.1-9.1)

2.1.3 Definition of Lease

Various writers and institutions have defined leasing differently. Some of which are cited as follows:

Leasing is an agreement that provides a firm with the use and control over assets without receiving title to them and this is the written agreement allowing

the use of the assets for a specified period of time, signed by the owner of the assets called the lessor and the user called the lessee (Hampton, 1994: 484)

A lease represents a contract under which one party is entitled to use an asset for a specified period. In consideration of this use, the user is required to make periodic payment to the owner of the asset. Stated differently, a lease is a contract between a lessor and lessee in which the owner of an asset allows another party to use it for a leasing fee (Rao, 1991: 797)

Conceptually, a lease may be defined as a contractual arrangement/transaction in which a party owning an asset/equipment (lessor) provides the asset for use to another/ transfers the right to use equipment to the user (lessee) over a certain/ for an agreed period of the time for consideration in the form of/ in return for periodic payment (rentals) with or without a further payment, Premium (Khan & Jain, 1999: 9.1).

2.1.4 Types of Lease

Lease may take different forms depending upon the terms and conditions agreed by the lessee and lessor. There are number of classification classified by different writers. Some important are presented as follows:

(A) Financial lease

Financial lease is a long-term lease on fixed assets that may not be cancelled by either party. Financial lease is basically the same kind of alternative as long term debt financing as per the point of view of source of financing (Hampton, 1994:485)

Financial lease holds following characteristics:

- a) The lease is non-cancelable.
- b) The lease is fully amortized.

- c) The lease does not include repair and maintenance services (Mathur, 1994:3)

The typical arrangement involves the following steps:

-) The firm that will use the equipment selects the specific items it requires and negotiates the price and delivery terms with the manufacturer or distributor.
-) Next, the user firm arranges with a bank or leasing company for the latter to buy the equipment from the manufacturer or distributor simultaneously executing an agreement to lease the equipment from the financial institutions. The term call for full amortization of the financial institution's cost plus a return on the lessor's investment. The lessee generally has the option to renew the option to renew the lease at a reduced rental on expiration of the basic lease but does not have right to cancel the basic lease without completely paying off the financial institutions (Weston and Copeland, 1991: 996-997)

(B) Operating leases

Operating lease is generally, short term, cancelable lease. Operating leases sometimes called service lease, generally provide for both "Financing" and "Maintenance Service".

Following are the key characteristics of operating lease:

- (i) Operating leases are not fully amortized. It means that rental payments required under the lease contract are not sufficient for the lessor to recover the full cost of the asset. The lessor expects to recover all costs either by subsequent renewal payments, by re-leasing the asset to other lessees, or by selling the asset.

- (ii) Operating lease often contain a cancellation clause. Therefore, the lessee has the right to cancel the lease and to return the asset before the expiration of the basic lease agreement.
- (iii) The lessor runs the risk of obsolescence.
- (iv) The term of this type of lease is shorter than the asset economic life. (Brigham, Gapensaki and Eterhardt, 1001: 736-737).

(C) Sale and leaseback lease

This is a special lease arrangement in which a firm (A) sells an asset to another firm (B) and simultaneously the two firms enter into a financial lease by which firm B leases the asset to firm A. as a result, the seller receives the purchase consideration for the asset and also retains the use of the asset in return for periodic payments. (Chandra, 1994:869)

(D) Leveraged lease

Under a leveraged lease arrangement, the lesser borrows a portion of the purchase price of the asset from a lender, which is typically a commercial bank or a financial institution. The asset and the lease payment secure the loan. The lender is paid back from the lease payments often directly by the lessee-the surplus left after satisfying the claims of the lender goes to the lesser. As the owner of the asset, the lesser is entitled to tax shelters associated with ownership. (Chandra, 1994:869)

(E) Direct Lease

Under a direct lease, the lessee identifies the asset it requires and either leases it directly from the manufacturer or else arranges for a leasing company (or finance company or commercial bank) to buy it from the manufacturer and then enters into a financial lease contract with the lesser. (Finery, 1989:374)

Besides above lease arrangements following other types are also existed.

-) Domestic lease
-) International lease
-) Import lease
-) Cross-border lease

2.1.5 Types of assets that can be leased

A firm can lease almost any kind of asset needed to conduct its business. Firms lease land, building and even factories with all their equipments. Manufacturers with a desire to make sales to customers that are short of cash encourage leasing and may even help a customer make arrangements to lease. (Hampton, 1994:486). Normally two types of assets are preferred for leasing. One is the asset having high cost like land and building, heavy equipments, airplanes etc and another the assets in which technology changes rapidly such as computer, television, medical equipments, vehicle etc.

Advantage of the lease to the lessee

The success of any business depends upon the level of need satisfying capacity of the offered product or service. Therefore, points of advantage that the lessee may get should be studied. Here are some advantages of leasing to the lessee.

) Financing of the capital good

Lease financing enables the lessee to have finance for huge investments in land, building, plant, machinery, and heavy equipments and so on without requiring any immediate down payment. Thus the lessee is supported to commence his business.

) Additional source of financing

Leasing facilitates the acquisition of equipment, plant and machinery without the necessary capital outlay and this has a competitive advantage of mobilizing the scarce financial resources of the business enterprises. It enhances the

working capital position and makes available the internal accruals for business operation.

) **Less costly**

Leasing as a method of financing is less costly than other alternative available.

) **Off balance sheet financing**

Neither the leased asset nor the lease liability is depicted on the balance sheet except that the fact of lease arrangement is mentioned by way of a footnote. Lease financing, therefore, does not affect the debt raising capacity of the enterprise.

) **Ownership preserved**

Leasing provides finance without diluting the ownership or control of the promoters. As against it, other modes of long-term finances, viz; equity or debenture, normally dilute the ownership of the promoters.

) **Avoid conditional ties**

Lease finance is considered preferable to institutional finance, as in the former case, there are no strings attached. Lease financing is beneficial since it is free from restrictive covenants and conditional ties, such as, representations on the board, conversion of debt into equity payment of dividend, and son on, which usually accompanies institutional finance and term loans from banks.

) **More flexible**

The lease rentals can be structured to accommodate the cash flow situation of the lessee, making the payment of rentals convenient to him. These rentals are so tailor- made that lessee is able to pay rentals from the funds generated from

operations. The lease period is also chosen so as to suit the lessee's capacity to pay rentals can considering the operation lifespan of the asset.

) **Simplicity**

A lease finance arrangement is simple to negotiate and free from cumbersome procedures with faster and simple documentation. As against it, institutional finance and term loans require compliance of covenants and formalities and bulk of documentation, causing procedural delays.

) **Tax benefits**

By suitable structuring of lease rentals, a lot of tax benefits can be derived. If the lessee is in a tax paying position, the rental may be increased to lower his taxable income. If the lessor is in tax paying position, the rentals may be lowered to pass on a part of the tax benefit to the lessee. Thus the rentals can be adjusted suitably for post payment of taxes.

) **Avoidance of obsolescence risk**

In a lease arrangement, the lessor being the owner bears the risk of obsolescence and the lessee is always free to replace the asset with the latest technology. (Khan & Jain, 199; 9.6-9.8)

2.1.6 Advantage of Lease to the Lessor:

) **Tax benefit**

The greatest advantage for the lessor is the tax relief by way of depreciation. If the lessor is in a high tax bracket, he can lease out assets with high depreciation rate and thus reduce his tax liability substantially. Besides the rentals can be suitably structured to pass on some tax benefits to the lessee.

) High profitability

The leasing business is highly profitable since the rate or return is more than what the lessor pays on his borrowings. Also the rate of return is more than in case of lending finance directly.

) Full security

The interest of lessor is fully secured since he is always the owner of the leased asset and can take repossession of the asset, if the lessee defaults. As against it, realizing an asset secured against loan is more difficult and cumbersome.

) Trading on equity

Lessors usually carry out their operations with greater financial leverage. That is they have a very low equity capital and use a substantial amount of borrowed funds and deposits. Thus the ultimate return on equity is very high.

) High growth potential

The leasing industry has a high growth potential. Leasing financing enables the lessees to acquire equipment and machinery even during a period of depression since they do not have to invest any capital. Leasing thus maintenance the economic growth even during a recession (Khan and Jain, 1999: 9.8-9.9)

2.1.7 Limitation of Leasing

-)** Most of the growth of leasing was due to the fact that it was an off balance- sheet method financing. Critics of leasing have strongly argued that leasing is only a disguised form of debt financing. Donald Gant says, “Lease financing is then essentially a form of borrowing-perhaps borrowing an asset rather than the funds with which to purchase it, but resulting in obligation which substantially the same as those incurred in debt are financing.” He further

advances his argument by saying that after all, we have seen that lease financing results in an assumption of capital risk on the part of the company and with it an objection similar to that imposed by debt, it would seem then, that whether the company uses its credit in the form of direct borrowing or to support lease commitments the total amount of its obligations will be the same. There is evidence to believe that leasing is regarded by the business community only as another form of debt. In a survey carried by Vancil and Anthony in USA in 1959 indicated that maximum respondents regard leasing as an intermediate form between secured debt and unsecured debt. Further, off balance sheet in so far as the balance sheet is placed before a financial analyst has no relevance, as accounting rules in most of the countries require disclosure of lease in lessee's balance sheet.

-) In most of the cases, leasing may be costlier than a straight borrowing because the lessor is only a financial intermediary and himself borrows from the market at prevailing or higher borrowing rates to which he adds his own profit also.
-) When rate of depreciation is quite high, taking assets on a lease may results in loss of tax benefits particularly when the asset is being acquired towards the year-end. Had the company bought the asset rather than leased in it, it would have claimed a full year's depreciation under tax law.
-) As, at the termination of lease period, the asset reverts to the owner, the lessee loses his claims on the residual value. At times, the equipments may have much higher residual value that what was provided at the inception of lease, so that lessee loses a substantial ownership benefit. The sale of residual is sometimes protection against inflationary erosion of money value.

-) Leasing does not provide the lessee the pride of ownership. Many people would not be satisfied merely by the right to use, which is provided under lease. They psychologically crave for ownership.
-) The lessor himself finances the lease by funds borrowed from banks and financial institutions and the leased asset is hypothecated to the banks. In case the lessor fails to meet his obligation to banks, banks shall seize the asset, causing loss to the lessee.
-) Leasing as a mode of finance is limited in equipment needs only; it cannot help a company secure working capital.
-) An environment of uncertainty prevails in the leasing industry, which is still at fledging stage. (Kothari, 1991:16-18)

2.2 Legal Provisions relating to Leasing Business

Tax Consideration in Leasing

Leasing makes sense whenever the parties to a lease contract face different managerial tax rates because leasing is primarily a tax driven means of financing. (Kean., 1995:641). Taxes play a very important role in structure of lease and in the value of leases to both the lessor and the lessee. (Roa, 1991:801). Considering the impact of leasing in a macro economic perspective, Government or Governmental agencies issue certain guidelines regarding leasing. These guidelines are very important for the deal of leasing.

Guidelines issued by Internal Revenue Service (IRS) USA are important to consider. The explanation is given in following sections.

The full amount of the lease payment is tax-deductible expenses for the lessee provided the IRS agrees that a particular contract is a genuine lease and not simply installment loan called lease. This makes it important that a lease contract be written in a form acceptable to IRS. A lease that complies with all IRS requirements is called guideline or tax oriented lease and the tax benefits

of ownership (depreciation and any tax credit) belong to the lessor. The main provisions of the tax guidelines are as follows.

-) The lease term (including any extensions or renewals at fixed rental rate) must not exceed 80 percent of estimated useful life of the equipment at the commencement of lease transaction. Further the remaining useful life must not be less than one year.
-) The equipment's estimated residual value at the expiration of the lease must equal at least 10 percent of its value at the start of the lease. This requirement can have the effect of limiting the maximum lease term.
-) Neither the lessee nor any related party can have the right to purchase the property at a predetermined fixed price at the lease's inception. However, the lessee can be given an option to buy the asset at its fair market value.
-) Neither the lessee nor any related party can pay or guarantee payment of any part of the price of the leased equipment, other than through lease payments.
-) The leased equipment must not be "limited use" property, defined as equipment that can only be used by the lessee or a related party at the end of the lease.

The reason for the IRS's concern about lease term is that without restrictions a firm could set up a "lease" transaction calling for very rapid payments that would be tax benefits. The lease that does not meet the tax guidelines is called a non-tax oriented lease. For this type of lease, the lessee (i) is the effective owner of the leased property (ii) can depreciate it for tax purpose and (iii) can deduct only the interest portion of each lease payment (Brigham, Gapensaki, and Etrhardt, 1001: 738-739).

2.3 Services of Value in Leasing

Following are the factors that give rise to leasing being a thing of value in the capital market.

) **Effects of differing taxes**

The dominant economic reason for the existence of leasing is that companies, financial institutions and individuals derive different tax benefits from owning assets. The greater the divergence in these benefits, the greater would be the attraction of lease financing, all the other things staying the same. The tax benefit associated with owning an asset is the tax shield afforded by the deduction of depreciation over the depreciable life of the asset. If the effective tax benefits associated with owning an asset were the same for all economic units in the economy and if capital markets perfect in every other way, debt and lease obligations valued in the same manner. As a result, their cost would be the same. If the lessor did not lower lease payments to give the lessee all the tax benefits of ownership, the prospective lessee could simply purchase the asset and finance it with debt. In this way, it could avail itself of all the tax benefits. Therefore it is not the existence of tax per se that give rise to leasing being thing of value but it is a situation in which different companies, financial institutions and individuals have different abilities to realize the tax benefits. Such differences are due to:

) Different tax rates among economic units in the economy:

Examples: differences in personal and corporate income tax rates and differences in tax rates among various individuals and corporations.

) Different levels of past and current taxable income among economic units: Examples: a company that carries forward a tax loss and pays little or no taxes.

) Different effects related to the alternative minimum tax: The presence of the alternative minimum tax (ATM) causes divergences in the ability of different corporations and individuals to fully use depreciation and the deduction of interest as expenses. Example: a company with redundant tax deductions will have an incentive to lease finance because the lease payment is not classified as preference item when computing the ATM. Companies not so affected will have an incentive to act as lessors.

A company that pays little or no taxes may lease an asset from another party that pays higher taxes. The lessee gets part of the tax benefits of ownership because its lease payments are lower than they would otherwise be. In turn, the lessor is able to use the full tax credit, which might not otherwise be available to it. As a result, both parties gain.

) **Leasing Financing in Perfect Capital Markets**

If the capital markets are perfect, there are no transaction costs, information is costless and readily available to all, securities are infinitely divisible, there are no bankruptcy costs and there are no taxes. Under such condition, the debt and lease obligation of a firm will be valued by secured lenders and lessors in the same manner. The cost of debt and lease financing will therefore be the same and the firm would be indifferent between these two methods of financing.

If the capital market is imperfect, debt and lease instruments may not be valued in the same manner. The imperfection of transaction cost, information cost, and less than infinite divisibility or securities do not have systematic effect in the sense that they favor lease or debt financing all of the time. Rather arbitrage between the markets is impeded; consequently, it may be possible for the firm to take advantage of the situation by issuing one type of instrument or the

other. Because the advantage is likely to be small and difficult to predict in practice.

) Bankruptcy costs to the lender or lessor

If a lessee or borrower liquidates, the lessor's position is somewhat superior to that of supplier of capital, the lessor owns the asset and can retrieve it when the lessee defaults. The lender finds it more difficult and costly to gain possession when the borrower defaults, even though the loan was secured with the asset.

The riskier the firm that seeks financing the greater the incentive for the supplier of capital to make the arrangement a lease rather than a loan. Many suppliers of capital are either lenders or lessor but not both. In some cases, loans are converted to leases when the risk of default has increased significantly. To the extent that any of the ex-ante costs of bankruptcy avoidable by lease opposed to debt financing are passed on to the lessee in the form of lower lease payments than otherwise would be the case a company might have an incentive to lease as opposed to buy/ borrow.

) Market Equilibrium Process

How much realization of the tax benefits the lease is able to achieve depends on the supply and demand conditions in the market for lease financing. A lessor unlikely to give up all the tax benefits, because realization of such benefits depends on its favorable tax situations. By the same token, competition among lessors will ensure that parts of the benefits will be transferred to the lessee in the form of lower lease payments than would otherwise be the case. The exact sharing of the tax benefits is negotiable but it will depend on equilibrium conditions in the capital markets.

Economic benefits passed off to the lessee are reflected in the implied interest cost of the lease. By concentrating on this cost and the economic benefits associated with leasing relative to those for growing the firm he is able to

determine whether lease financing is promising. In this way, the decision will be grounded in sound economic reasoning as opposed to the sales pitch used by many leasing company to sell its financing service.

) Other Alleged Advantages

In addition to above reason, there may be other reasons for existence of lease financing. For one thing, the lessor may enjoy economies of scale in the purchase of assets that are not available to the lessee. Also the lessor may have a different estimate of the life of the asset, of the residual value, or of the discount rate than the lessee. Moreover, the lessor may face different borrowing costs than the lessee. Finally the lessor may be able to provide expertise to its customers in equipment selection and maintenance. (Van Horne, 1001:556-558)

Accounting for Lease

The concern for a proper accounting method for leasing transactions exists in almost all the countries where leasing have passed a certain phase of development. The problem of the lease accounting in the western has been looked at mainly from a point of view of a lessee i.e. from the point of view of distortions likely to be caused in the lessee's balance sheet, if the assets taken on lease are not disclosed there in. in fact the problem has both the facets- lessor accounting as well as lessee accounting. The accounting problem for lessor is income recognition, whereas that for the lessee is asset recording. If the normal method of accounting is applied to record the leasing transaction, this intention does not appear in the statement made by the lessor and lessee. Failure to disclose long-term lease obligations in the balance sheet has the effect of distorting the true and the fair view of the states of affairs of the company.

) **Method of Accounting for Lease**

The method of accounting for lease differs country to country. The main methods that are prescribed and followed in different countries are as follows:

-) Finance methods, which is applicable in the countries following accounting standards similar to the SFAS-13 and IAS-17 to all finance leases.
-) Operating method, which is applicable to the countries following accounting standards similar to the SFAS-13 and IAS-17 to all operating leases. In countries, which do not subscribe to IAS or SFAS, this method is used for recording all types of leases.
-) Hybrid method that is followed for recording finance leases in some of the countries.

) **Finance Method**

The IAS-17, FAS-13, SSAP-11 etc, are required finance leases to be accounted for under the popularly called finance method according to which the lease is reckoned as financing transaction. Under finance method lessor and lessee keep record as follows:

Accounting by the lessee

As the lessee derives an equitable ownership in the asset at the very inception of the lease, he must capitalize the asset on his balance sheet. In order to distinguish the assets taken on lease from other asset, the leased asset may be shown separately. Parallel to the equitable acquisition of the asset, there is a long-term liability to the lessor in the form of contracted rental payments. The lessee must depreciate the leased assets as per his normal depreciation policy, and so he cannot take aggregate rentals to the debit of his profit and loss account. As a lease is considered akin to a loan, so are the lease payments

considered of compromising both interest and principle elements. Thus the lessee shall charge only the interest element, which is his real expense.

Accounting by the lessor

Under the financing method as the legal form of deal is ignored and the lessor is supposed to have no equity over the asset, the lessor does not capitalize the asset on his balance sheet, what the lessor debits is the amount that is receivable from the lessee by the way of lease rentals, because that is what he really owns. Thus the features of the accounting by the lessor are:

- a) The lessor shall not capitalize the asset on his balance sheet.
- b) He will show as a current asset the lease receivables. The receivables may show at the agreement value less finance charges, which have not yet matured. Alternatively, the receivables may show as a gross receivable, the finance charges not yet matured being shown as a current liability.
- c) The lessor's income statement is credited every year with the interest element in-built in the lease rentals.
- d) The lessor does not depreciate the asset in his books.

Operating Method

Since operating leasing is not existed in Nepal, this method is not studied in detail.

Hybrid Method

The hybrid method of lease accounting attempts to combine the legal treatment as also the financial reality. The objective has been to avoid conflict with the common law and tax statutes. Accordingly, the lessor is permitted to capitalize the asset, and the lessee must disclose the assets taken on lease by way of note to its accounts. The lessor may take the rentals to his income but should charge depreciation in a way that the resultant post depreciation profit is equal to the finance charges under the financing method. The hybrid method is doing

conveniently in many countries where leasing has not come to a very advanced stage, or where tax authorities have not accepted the dichotomy between the accounting treatment and the tax treatment (Kothari, 1991: 488-510).

Accounting treatment in India

Presently the accounting treatment of lease transaction in India as follows:

-) The leased asset is shown on the balance sheet of lessor's book.
-) Depreciation and other tax shields associated with leased asset are claimed by the lessor.
-) The entire lease rental is treated as income in the books of the lessor and as expenses in the books of the lessee. (Chandra, 1994:871)

Evaluation of Lease Agreement

Whether to go or not to go for leasing is like an investment decision. Leasing is judged under NPV or IRR method. The NPV for both the party should be positive to involve in the agreement.

Lessee evaluates the project by comparing capital preserved plus the discounted lease rental benefit minus discounted opportunity cost of not owning the asset minus discounted lease rental minus discounted residual value. In this calculation negotiating variables are lease rentals and residual value only. Therefore for lease contract, lessee calculates lease rental where NPV is zero which would be in turn be possible highest benchmark of lease rental for lease agreement to be acceptable for lessee.

Similarly, lessor calculates NPV by taking difference of discounted lease income and associated benefit of owning the asset over the initial cost involved in buying an asset and other related cost discounted by rate of return. For negotiation, lessor calculates lease rental making NPV equals to zero, which

would be in turn, be the minimum lease rental at which lessor would just receive required rate of return.

Through the calculation, minimum lease rental benchmark for lessor and maximum lease rental benchmark for lessee would be estimated. Agreement would be feasible, if the minimum lease rental calculated by lessor is less than the maximum lease rental calculated by the lessee. The margin between these two gives the room for negotiation; otherwise, the agreement between the two parties could not be feasible.

Things to be considered while leasing

) Default by the lessee

The chances of default are present in leasing as well. The chances of lessee not paying the lease rental present as in case of loan. Therefore, in lease rental calculation, though unlike in loan the lessor holds title of the asset; the default risk is to be incorporated.

) Different charges associated with lease contract

Different charges such as maintenance, insurance etc are associated with lease contract. These responsibilities involve cost and directly affect the lease rental to be calculated either by lessee or lessor.

) Renewal Option

A lease provision allowing the lessee, at its option, to renew the equipment lease for a rental rate predetermined at lease inception that is substantially lower than the expected fair market rate at the date the option can be exercised.

) **Purchase Option**

A lease provision allowing the lessee, at its option to purchase the equipment for a price determined at lease inception that is substantially lower than the expected fair market value at the date the option can be exercised.

) **Conditional Sale**

Also known as security agreement. An agreement with an option to purchase the leased property at the expiration of the lease term at a bargain purchase price. This purchase price is predetermined, and the user of the equipment is treated from the start as the owner of the equipment.

) **Residual Value**

The value of an asset at the conclusion of a lease. The residual value being future value, it can be, at best be estimated only. This estimation at large determines benchmark of lease rental to be decided by both lessee and lessor.

) **Useful or economic life**

The period of time during which an asset will have economic value and be usable. Useful life of an asset is sometimes called economic life of the asset.

) **Payment Schedule**

This includes deciding in advance whether the payment has been made in advance or in arrears.

) **Required rate of return**

Lessor determines lease rental by discounting the future cash flows by required rate of return, whereas lessee discount the future cash flow by the cost of capital. In both the case, it needs to be taken care that required rate of return varies with time, either, agreement should reflect that the lease rental is subject

to change in market or sufficient cushion be provisioned for such changes while deciding lease rentals. (Training Manual, Bankers Club NRB)

2.4 Origin of the concept of the leasing

The concept of leasing is traceable to old writings. Leasing was adopted in real estate. Historians claim origin of operating leasing to the age of Sumerians before 1000 B.C. for agriculture implements and hand tools. Leasing of farmland in the early civilization of Babylonia around 1800 B.C. and Greece around 370 B.C. The concept continued developing and its coverage went on increasing from immovable to moveable like equipment, ships or vessels, or domestic animals like ox and cows, etc. Most phenomenal growth in leasing was noticed around 19th century when many firms took to leasing of railway wagons in the United Kingdom in the 1840s. These firms were known as wagon companies. One company established in 1895 which switched over its functioning to leasing railway wagon to coal and mine owners for fixed returns.

Leasing developed on similar pattern in the United States of America. In the last of the 19th century, the railroad and railcar manufacturers were under capitalized and unable to finance rail cars, which were not available through conventional lending sources. Equipment trust certificate was evolved to evidence security interest in the equipment, which was similar to non-tax oriented equipment lease in use today. Such rail car financing aided the growth of Industrial revolution by providing railroads as means to expand their services of getting goods to and from market world and the United States. Post World War II reconstruction of the European countries much depends upon leasing financing using equipment trust certificate.

From 1950s the development of airlines was done only through the use of lease financing in the USA for acquiring aircrafts from the manufacturers. In 1960s, true lease came into vogue, which had stimulant on account of favorable tax laws in 1963. Thus, by slow and gradual paces, leasing has become one of the

important means of financing the project cost of the industrial enterprises, procuring consumer durables for family dwellings for better life standards, etc. It is being used of both lessor and lessee.

In May 1951, the United States leasing corporation was set up followed by Canadian subsidiary- Canada Dominion Leasing Corporation in June 1959. In 1960s Mercantile Leasing Co. was established in London by Mercantile credit Co. And, thus, the leasing activity spread in Western European nations like France, Italy, Germany, etc. In 1963, one of the largest leasing company in the world known as Orient Leasing Co. was established in Japan. It spread to other parts of the world. Leasing afforded as a marketing device helping the manufacturers to retain control of the market and customer.

In India, leasing was developed in modern sense as a professional financial service with the start up in 1973 by the first leasing company of India set up in Madras. In 1980s onwards as much as 500 leasing companies were noticed in existence. (Verma, 1994: 1)

2.5 Growth of Leasing in Developed Nations

There have been two principal reason which contributed to the development of equipment leasing in the developed countries, namely (i) the high rate of technological obsolescence of most of the industrial equipments which made “use of the equipment” through leasing a better proposition than ownership; and (ii) the earning capacity of the equipment had primary importance to the psychological factor of ownership. Government in the developed nations also encouraged the equipment-leasing concept by providing specific monetary and fiscal incentives for companies to lease out equipment.

Leasing is rapidly becoming a more and more pronounced part of financing industrial development of all industrialized capitalist countries. The UN paper on leasing cited the financial data that go to establish the importance the companies gathered in these nations. According to the UN paper, leasing is an

important new method of financing and dates back from the times since the Second World War. Lease firms play a role analogous to that of banks and other independent financial institutions, but act by buying and then leasing equipment to their clients rather than loaning them money to buy it. Some manufacturing firms have already introduced leasing by establishing subsidiary or captive leasing in the marketing of their own goods. The first independent leasing company was the United States Leasing Company incorporated in 1951. it proved successful, and the industry spread to England, with the establishment of the 1960s, leasing industries were flourishing throughout Western Europe, the United States of America and Japan. Financial institutions with long standings established the equipment leasing companies due to partly attractive profitable leasing business varying legal treatment; circumstances and tax policies have made leasing more appealing in some countries than in others. Circumstances and policies also affect the precise forms the leasing tends to take, or can take, and in what situations it can be applied. For example, in Austria Financial leases on real estate accounted for one fourth of the growth of leasing industry in 1979-1980, whereas elsewhere this is rare.

Leasing covers mainly the transactions in industrial goods, in Western Europe, about one third of leasing business is devoted to automobile leasing and another third to industrial machinery. About one fifth of the business represents computers and office machines, with the rest divided up among ships, aircraft, railroad rolling stock and other miscellaneous. The distribution in Australia and china is approximately the same. The automotive portion in Australia is a bit larger, and in Canada the industrial portion is smaller but the aircraft portion is larger. In Japan however computers and office machines represent more than two third of the market, about one fifth relates to industrial machines and the rest is miscellaneous equipment. Leasing in some developed nation is discussed below.

A. United States of America

America has largest financial leasing industry in the world. It has been significantly influenced by tax policy particularly ever since 1981 Economic Recovery Tax Act was adopted giving lessor and lessee new platform for negotiation. Another feature of American tax law is that certain tax benefits generally available to lessor may be lost if the leased property is used outside the United States. The phenomenal recent growth in leasing in United States of America is almost exclusive attributable to the generous treatment of leasing by the Act and the new “safe harbour” leasing rules adopted by United States tax authorities. It is called “safe harbour” leasing because United States taxing authorities have indicated that they will not challenge leased structured within their guidelines. Besides this, Tax Reform Act 1986 has added more attractions to leasing business. Alternative Minimum Tax (AMT), changes in depreciation schedule, intense competition grapping the leasing industry, availability of computer based software packages etc are some of the present day main feature of lease business in USA.

B. United kingdom of Great Britain

Leasing in the UK has been among the fastest growing commercial activities in the past two decades. The major users of lease finance were manufacturing, transport, agriculture distributives and others, service industry. Major lease financiers have been the leasing subsidiaries of major banks and finance houses. In the UK every large company would be utilizing leasing as a means of acquiring some proportion of its capital equipment requirement ranging from a typewriter to whole chemical or engineering complex. Leasing companies covers the entire area of capital equipment. The UK Government has been very positive in its attitude to leasing, particularly towards encouraging leasing companies to re-equip and therefore, to become more profitable and more competitive on an international basis. They have made it possible for all the tax allowance and grants available to the user (lessee) to flow directly to the lessor.

Leasing in the UK like USA is primarily tax-based and used by both lessors and lessees to achieve tax savings. The basic pattern of the tax-based leasing system is as follows: the lessor, as the owner of the asset leased, is entitled to a very generous “capital allowance” entitling him to deduct the entire cost of the leased property during the initial period; the lessee is entitled to deduct his rent payments from his income as current expenses. Thus the lease form will be attractive to a user/ lessee whose taxable income would not be sufficient to take advantage of the capital allowances. The benefit of capital allowance to the lessor will usually be reflected, by a reduced rental payment to the lessee that is more favorable than alternative financing.

Leasing had developed in UK only after 1960s and gathered momentum only in 1967-69 within the period of credit restrictions. In this period, commercial banks has been on look out for entering the leasing operations by acquiring controlling interests in the prominent finance but non-banking companies who had been engaged in hire purchase and leasing activities. Subsequently, these banks had restructured their activities. After that leasing became so popular that a number of “big ticket” contracts were entered into by consortia and partnership and number of banks combined to form Air Lease international to finance the reequipping the world airline and shipping lines.

In 1971, Finance Act provided the relaxation that helped in accelerating the growth of lease industry. Initially 60 % of the cost of acquisition was treated as “capital allowance” deductible for the tax purpose in the year of acquisition or carried forward at the discretion of taxpayer, in whole or part, against future projects. In the following years, the taxation reflects was extended to 100% of the acquisition cost of business assets. The gain of this policy has been that leasing company becomes the purchaser and is entitled to the capital allowance. In case the leasing company has taxable profits to take advantage of capital allowances the benefits of the allowances will be passed on to the lessee company in rentals. This is the reason that major banks in UK entered into leasing to take benefits of capital allowances out of the profits they generate

from the entire banking business. Besides, development grants are also available and leasing company may obtain this benefit provided the assets are used by lessee company designated area. The benefits the UK banks availed include (i) taxation relief of capital allowance (ii) convenience and comparative safety of fixed contracts with built-in security and regular rental cost flow (iii) opportunity for using fund (iv) offering customer an attractive alternative source of finance; and (v) leasing can be done for non customer of bank as no continuing relationship is required for availing of the benefits.

C. West Germany

In recent years, the leasing industry of West Germany has played an important role in the achievement of investment plans. German laws give separate treatment to operating and financial leasing. General commercial law, as usually provided by manufacturing companies who act directly as lessors, regulates operating leasing. Financing leases on the other hand is regulated pursuant to a decree issued by the Federal Minister of Financial affairs on 19 April 1971. Cross border leasing is very little in West Germany but indirect international leasing do exist. Majority of the leasing finance is restricted to domestic transactions.

D. France

French lease market has been growing continuously. The most active areas were computers and electronic equipments, trucks, specialized industrial equipment and machine handling and public works equipment. Operating lease in France is not so developed.

No better tax status is available in France to lessor as is available in United Kingdom or the United States. It is only the traditional inherent advantages of the leasing concept- flexibility, strong security, low capital requirements that suffice to drive the lease industry forward in France.

The French leasing market is highly segmented. It is regulated by a 1986 law, which gives it the name of “credit bail mobilizer”. There are no attractive tax benefits from leasing but depreciation schedules are generous. Cross border leasing is still rare.

E. Japan

Experienced rapid growth. Main stress was laid down on its development in 1970s. Leasing companies have been set up with the support of commercial banks, general trading companies and large manufacturing firms, for the banks the development of leasing represented a diversification of the services, which they could offer to their client. For general trading companies and large manufacturing firms, leasing was a means of promoting sales while at the same time reducing financial burden and the risk, which they had borne in the past. These factors encourage, banks, trading firms and manufacturers to invest in leasing companies.

Although there is no special legislation governing the modern financial equipment lease in Japan, yet leasing industry has experienced significant growth. The legal relationship is construed between the parties involved in accordance with lease contract between a leasing company and a lessee and the sales contract between the leasing company and the seller. Thus there are two different contracts between the three parties. Leasing company enters into two separate contract viz., one with the firm selling equipment and the other with the lessee.

Most leasing companies in Japan deal with the financial lease transactions in the manner as follows:

-) A lessee chooses equipment and the seller.
-) The lease contract is concluded between the lessee and the leasing company.

-) The sales contract is concluded between the leasing company and the seller.
-) The seller tenders the equipment to the lessee.
-) The lessee examines the equipment and if the nature or the content of the equipment fulfill the necessary conditions of the contract, he gives his willingness thereof to the leasing company.
-) The leasing company pays the price to the seller.

Thus the lease contract gets completed and formalized.

The lease contract covers following special provisions:

- a) The nature of lease is non cancelable and the lessee may not terminate the lease contract in the middle of the term of lease.
- b) The leasing company does not take any responsibility for the delay of delivery of the equipment or its defects and
- c) The leasing companies do not bear the risks of loss or damage of the equipment.

On the other hand, the sales contract covers the assignment of the right from the leasing company to the lessee to claim compensation for damages against the seller until the lessee hands over a receipt to the leasing company. This is so because it is the responsibility of the seller to ensure the leased equipment to the lessee in perfect condition as the seller bears the risk of loss or damage of the equipment. (Verma, 1994: 15-13)

2.6 Leasing in Developing Nations

Growth of leasing as compared to developed nations has been slow in developing countries. But it is now established as a growing industry in many such countries. Development of leasing in some of the developing countries has been discussed below:

A. Brazil

Leasing industry has grown in Brazil because of governmental regulations, which patronize only financial lease. The operating lease are not in vogue in Brazil, as government has put no efforts to cover them under regulatory control. Central bank of Brazil exercises control and regulates the activities of leasing companies because of the financial character of leasing, as essentially it is a financing method. As such only leasing companies authorized by the central bank of Brazil are permitted to enter into leasing business. This checks the growth of foreign companies doing leasing business in the country. The Central bank of Brazil has established strict guidelines for both the internal operation of leasing companies and required provision of lease agreements. Some of these provisions are stated below:

- A. The debt of leasing companies may not exceed 15 times the capital plus reserves.
- B. At least 70% of all lease agreements must be entered into with Brazilian controlled corporation.
- C. A single lessee may not represent more than 10% of a leasing company's receivable.
- D. A leasing company, which desires to maintain more than 10 branch offices, must have additional capital for each new branch office.
- E. The law requires that lease agreements contain the following provisions:
 - a. The lease terms must be at least three years, in the case of automobiles, however the term must be at least two years.
 - b. A complete description of leased goods.
 - c. The value of rental payments.
 - d. The right of the lessee to choose at the end of the contract period to renew the contact, to purchase the leased good or to return it. The agreement may stipulate a guaranteed minimum residual value of the leased goods.

- e. A stipulation as to what method will be applied to the rental payments and sales opinion in order to account for monetary devaluation.
- f. A price or criteria (such as market value) for exercising the option to purchase such an option may not be exercised, however, before the contract period is terminated.
- g. The designation of the rights and obligation of the contracting parties, including the regulations of additional charges and expenditures, the improper use of leased goods, insurance terms, obligations resulting when damage is caused by third parties or when there are defects in the leased goods, provisions for substitutions, inspection and maintenance of a leased goods, etc.

To boost overseas leasing business, Brazil had adopted a legal structure in 1981 for import leasing by which it expected to allow for a greater amount of cross border leasing. Import leasing already covered such items like aircraft, ships and oilrigs, which were already being leased into Brazil. More ample participation by foreign lessors in the Brazilian market has also been made through the relaxed regulation for import leasing to cover equipment, computer or vehicle, the importance of which is authorized under existing regulations. The 1981 Brazilian import leasing law established the following conditions for leasing:

-) The non-existence of similar nationally manufactured equipment.
-) A minimum lease term of five years.
-) The total cost of leasing may not exceed the price of a comparable import- financing alternative.
-) Payments must be distributed equally during the term of lease. The terms are attractive to lessors based in developed nations like multinational companies.

B. Republic of Korea

In South Korea, leasing industry law adopted in 1973 which governs basically the finance leasing, a dominant leasing method in the country. Leasing finance has been promoted since the enactment of leasing industry law in 1973. The leasing regulations were revised in 1976 with the assistance of international finance corporation to provide greater flexibility for the parties and to clarify the distinction between lease and installment sales. After the revision, significant growth in the leasing industry was noticed in the country. Leasing has grown more rapidly than originally anticipated in 1976. In 1976, new equipment financing through leasing accounted for 1.3 percent of private fixed capital formations as compared to 0.4 percent in 1976. In 1980, this share had risen to approximately 1.5 %. The law gives enough protection to lessors in Korea to make them feel care free of the risk-less nature of the transactions. The lessor provides an alternative means of financing a user's equipment by advancing funds. Typically the lessee selects the suppliers and the leased property and the supplier delivers the property directly to the lessee. In most case the lessor does not inspect or verify the technical features of the leased property, which he has purchased. Besides, the terms of lease are flexible. The terms provide the lease to usually extent to 64 months while traditional bank financing would be available only between 36 and 60 months for similar equipment. Moreover the terms of bonds sold in the security markets usually extend to only 36 months. Fiscal considerations have also rendered it attractive to private enterprises that faced acute shortage of medium and long-term capital and are now serviced by leasing companies. Merchant banks have become more prominent in Korea in providing lease finance.

C. Thailand

Equipment leasing has only recently been introduced in Thailand. There is no legislative or administrative regulation to cover leasing business. Traditional tax structure is main hindrance in developing the leasing business. However,

international finance corporation has attempted to encourage leasing in Thailand by participation in the formation of leasing company. International Finance Corporation reports that the tax treatment applied to leasing companies is based on laws intended for traditional rentals of property and is not well suited for modern financial leasing. For example, a business turnover tax is charged on the total rental revenues of leasing companies instead of being limited to the interest portion of leasing companies' receipt. Besides, tariff and sales tax is applied to certain leasing transactions, which further reduce the competitive attraction of leasing as a method of financing. Recently the ministry of finance has authorized the board of investment to revise tax treatment of leasing transactions in the light of their essentially financial nature. With such amendments, leasing business is bound to become an attractive alternative method of financing.

D. Bangladesh

Leasing activities in Bangladesh commenced with the establishment of industrial development leasing company of Bangladesh Ltd in 1985. There are two or three private companies engaged in leasing plus hire purchase business of vehicles and household goods in small scale but they do not extend lease for industrial machinery and equipments. IDFC assumes full responsibility of developing lease market in Bangladesh through advertisement campaign direct contact with potential entrepreneurs direct mailing services and arranging meeting with members of the regional chambers of commerce and industries to familiarize the advantage of leasing.

Since leasing stands in its infancy in Bangladesh accounting principles for leasing have not been enliven so far by the accounting bodies. But operating method of account under which the leasing company capitalizes the lease assets and charges depreciation in the income statement is acceptable in both accounting and taxation. Lease Company has to declare the taxable income based on tax depreciation.

2.3 Review of Journal and Articles

Review from International context

Various numbers of research studies have been done internationally on the leasing. The findings of some of the research studies are mentioned below:

The study conducted by James. Van Horne on The Cost of Leasing with Capital Market Imperfection using a state- preference model demonstrated that it is useful to being by assuming that capital markets are perfect and complete. This implies that there are no transaction costs, information is costless and readily available to all, securities are infinitely divisible, there are no bankruptcy costs, and there are no taxes. Complete financial markets imply that the desires of borrows are satisfied with respect to the kinds of financial instruments available in the market. Under these assumption and the implied perfect competition among financial markets that results, it can be shown that the debt and lease obligations of a firm will be valued by secured lenders and lessors in the same manner.(Van Horne,1977)

the study conducted by Myron B. Slovin, Marie E. Sushka, and John A.polonchek on Corporate Sale and Leasebacks and Shareholder Wealth revealed that a company that pays little or no taxes may lease an asset from another party that pays higher taxes. the lessee gets part of the tax benefits of ownerships because its payments are lower than would otherwise be. In turn, the lessor is able to use the full tax credit, which might not otherwise be available to it. As a result, both parties gain. (Slovin, Sushka & Polonchek, 1990)

The empirically analyzed of the marginal tax rates paid by companies that lease and those that borrow has found that there is a negative relation between operating lease levels and tax rates and positive relation between debt levels

and tax rates. For capital leases, the relation is ambiguous. The evidence is consistent with tax-driven clientele when it comes to the lease versus buy/borrow decision. Low tax- bracket firms lease more and borrow less than high tax- bracket firms.(Graham, Lemmon and Schallheim,1998)

For a lease transaction to qualify as a lease for tax purposes, and for the lease to be able to deduct the lease payments, the life of the lease must approximate the life of the asset, and the lessee cannot be permitted to buy the asset at a nominal value. It is important to consult lawyers and accountants to insure that a lease is valid under current IRS regulations. (Weston & Brigham, 1992)

The discount rate used to calculate the present value of the lease payments must be the lower of

- a) The rate used by the lessor to establish the lease payments or
- b) The rate of interest which the lessor would have paid for new debt with a maturity equal to that of the lease. (Weston, 1992)

There are two factors, which will determine the lessor's profitability of leasing in year to come.

- i. the lessor's ability to tap cheap source of funds not available to his clients
- ii. His client's composition that may consists of people who find it difficult or inconvenient to tap the normal sources of finance available. (Kothari, 1999)

If the firm is unprofitable, or it is expanding so rapidly and generating such large credits that it cannot use them all, then it may be profitable for it to enter a lease arrangement. In this situation, the lessor (bank or a leasing company) can use the tax shield and give the lessee a corresponding reduction in lease charges. In recent years, railroads and airlines have been large users of leasing

for this reasons, as have industrial companies faced with similar situations.
(Vandewicken, 1973)

The risk is associated with the uncertain future net cash flows to be derived from employing the capital services of the assets. This risk is borne by the leasing company if the lease contract is cancelable at any time with no penalty, borne by the user firm if the lease contract is non-cancelable over the life of the asset, and shared by them under any contractual arrangement between these two extremes. But, competitive capital markets will ensure that the implicit discount rate in the leasing arrangement, as negotiated, will reflect the allocation of the risks under the particular sharing arrangement specified.
(Miller and Upton, 1976)

A study by Drury & Braund by why lessees prefer to lease rather than to borrow indicated that the leasing decision is not based purely on choosing the lowest cost alternative. The study indicate that firms find leasing attractive for the following reasons:

-) Lease finance can be obtained with greater ease and fewer restriction than other forms of finance.
-) Leasing is easier to arrange from an administrative point of view, than borrowing.
-) Lease can be arranged in which the rental payments increase over the lease period, thus enabling low rentals to be charged against profits in the early stages of a projects life.
-) Leasing provides a way to avoid capital expenditure controls.

Only by correctly valuing leases and comparing any negative net present value with an assessment of the qualitative factors can sound decision be made.
(Drury & Braund, 1990)

Leasing, particularly financial (capital) lease, may enable the firm to use the lease as a substitute for the debt- financed purchase of a given asset. Because of differing tax brackets of lessors and lessees, different tax treatments of leases and purchases, and different risks and borrowing costs for lessor and lessee, leasing may provide more attractive risk return tradeoffs to the firm than would result from using debt financing to purchase a given asset. (Gitman, 1988)

Review from Nepalese Context:

In this section, the previous research work done about the leasing business in Nepal is reviewed. Although there are not many research works found related to this topic, there are some studies found relevant to the topic of the researcher.

Mahat (2001) conducted research on the topic of “Loosing Leasing Companies” in the year 2001 while he was working for NSLMB, made a study about how the leasing companies are making loss despite showing accounting profit in the books of account. He states that despite the fair length of time has passed leasing business has not been able to get momentum. He further states that the leasing companies are paying taxes for the recovery of their own capital also, the capital portion of the lease rental, as the whole of the lease rental is treated as an income. But as against this, the lesser can claim depreciation on leased asset, which is being used by the lessee.

He further adds that over the period of lease, the tax benefit is equal to the tax loss, and if we consider the time value of money, then there is loss incurred. He states that the prevailing rate of the depreciation prescribed by the tax authorities discourages leasing business in Nepal. He concludes that the leasing has many potential in the development of the economic conditions of the country and states that the government should adopt soft and encouraging attitude towards the leasing industry at least in the initial stages.

Dhungyel (2005) after the completion of his survey, he concludes that the leasing business is in the stage of infancy and experimentation. He states that the leasing business has been overlooked within the Nepalese financial sector. He states that even the pioneers of the leasing business have not taken the leasing as the first priority. He adds that the lack of act relating leasing business has created ambiguity and has not facilitated the development of leasing business in the country. He found that the lease that the companies are providing is nothing more than a secured loan issued to the lessee. He further adds that the lessor/finance companies have more rights and less responsibility, whereas lessee has the less rights and more responsibilities.

His survey on opinion related finance companies/leasing business found that due to the high credit risk and lack of market, the finance companies are hesitating to enter the market. He further found that the majority of the finance companies feel that the existing infrastructure for carrying leasing business is not sufficient and are also not satisfied with the provision made by NRB regarding leasing business. He concluded that the machinery and tools for small and medium sale industries need to be focused to develop leasing business in the country.

2.4 Review of Previous Thesis

Joshi (2003) has made a study on equipment leasing business in Nepal- unpublished master's degree thesis on 2003/Feb, states that how the equipment leasing business is done. His main area of study were practice and procedures followed in course of leasing business and analysis of existing legal provisions related to the leasing business.

Shrestha (2003) in his study "Problem and Prospects of Leasing Business in Nepal" an unpublished masters' degree thesis TU 2003/ Feb, has made a thorough study on how the leasing business in Nepal are not able to get momentum although it pass a fair length of time. His study emphasis the absent

of leasing act is the major problem for leasing business. A part from that low professionalism is also the drawback identify by him.

Pathak (2004) in his unpublished Dissertation entitled "Leasing Business in Nepal" highlights how investors are safeguarded from concerned authorities, listed companies and associated investors organization and influenced to invest in the leasing business. He further adds that over the period of lease, the tax benefit is equal to the tax loss, and if we consider the time value of money, then there is loss incurred. He states that the prevailing rate of the depreciation prescribed by the tax authorities discourages leasing business in Nepal. He concludes that the leasing has many potential in the development of the economic conditions of the country and states that the government should adopt soft and encouraging attitude towards the leasing industry at least in the initial stages.

Adhikari (2005) has studied "Leasing Business in Finance Companies" an unpublished masters' degree thesis TU 2005. In Nepal leasing business is in its infancy stage. Many finance companies have established intending to perform leasing business. Out of them many companies have not even yet started that business. The main objectives of this research are: To study and analyze the introduction growth and development of leasing business in Nepal, To find the problems and prospects related to leasing business in Nepal, To study and examine the existing legal provisions relating to the leasing business in Nepal.

2.5 Research Gap

In this way, many researchers have studied about the leasing business in Nepal from different angles. Obviously the conclusion that they present is also varied according to focus, size of the sample and the methodology they followed but none of the researchers have studied about the "Technical Analysis of leasing business" in Nepalese context. It is therefore, a pioneering study, a contribution to knowledge on a vital aspect concerning investment decision and in order to overcome the different of past works and to fill up the research gap.

CHAPTER - III

RESEARCH METHODOLOGY

Research methodology is the process of arriving at the solution of the problem through planned and systematic dealing with the collection, analysis and interpretation of facts and figures. Research is a systematic method of finding right solution for the problem whereas research methodology refers to the various sequential steps to adopt by a researcher studying a problem with certain objective in view. In other words research methodology refers to the various methods of practices applied by the researcher in the entire aspect of the study.

This chapter contains a discussion about methodologies employed in order to achieve the objective of the research. To summarize the details going to follow, this chapter includes the population or universe of the research, sources of data, sampling procedures, how the data and information has been collected, how it will be presented in the analysis and limitations of methodologies.

3.1 Research Design

A research design is the arrangement of condition for collection and analysis of data in a manner that aims to combine relevance to the research purpose with economy in procedure. In fact, research design is the plan, structure and strategy of investigation so as to obtain answer of the research question and to control the variance.

This study evaluates the leasing business in Nepal. It covers the data from the year 2003/04 to 2007/08. To accomplish the objective adopted the descriptive Vs analytical type of research design. Descriptive approach is utilized for conceptualization, problem identification, conclusion and recommendation of the research. On the other hand, analytical approach is adopted for the

parametric and non-parametric test of the data. It described analyze all these facts that collected for the purpose of the study.

3.2 Population and Sample

The population or the universe means the total population of the sample. And the population for this study comprises of all the 59 finance companies of Nepal. However, for the specific purpose of the study only 4 finance companies performing leasing business are taken as the universe.

In Nepal there are altogether 59 non-bank financial institutions. Among which 36 finance companies are established and operating from inside the Kathmandu valley; 31 in Kathmandu city, 5 in Lalitpur and 1 in Banepa. And the other 11 finance companies are situated outside the Kathmandu valley.

For the purpose of analyzing the facts of the finance companies all the finance companies are taken into consideration. And for the purpose of the study of leasing business and its prospects, 4 finance companies operating leasing business are taken. Due to the fact that there are only four finance companies operating leasing business there is not much room to take sample from the population. However, sampling has been done taking location as its prime factor. Therefore, for studying in detail all 3 finance companies from within the Kathmandu valley are taken as sample for study. Sample companies from within the Kathmandu valley are International Leasing and Finance Company, Union Finance Company and Nepal Sri Lanka Merchant Bank. And for analyzing growth and uses of funds' purpose, one finance company located outside the Kathmandu valley is also taken into consideration and it is World Merchant Banking and Finance Company.

3.3 Data Collection Procedure

The study is focused on the problems that the finance companies face while operating leasing business in the country. For the purpose of fulfilling the data

required, various published and unpublished data were collected. The data collected were mostly primary data by intensive opinion survey and interviews with the concerned office personnel. Information was also collected by searching the World Wide Web.

3.4 Data Processing Procedures

The main objective of this study is to try to find the problems related to the leasing business in Nepal. So all the published and unpublished data are used as the primary source of information for studying and analyzing the past and current situation of leasing business in Nepal. Other journals, magazines, information on the web sites and publications of NRB were also used as secondary data for the studying and evaluating purpose. Finally, frequent interviews and interactions with the concerned office personnel were made to understand the problems and to find the solutions.

3.5 Data Analysis Tools

In the process of analyzing and evaluating various data different statistical tools has been used. In this study, statistical tools such as standard deviation, mean, coefficient of variation, coefficient of correlation between different variable as well as hypothesis test have been used, which are as follows:

i. Arithmetic Mean or Average (\bar{X})

An average is the value, which represents a group of values. It depicts the characteristic of the whole group. It is an envoy of the entire mass of homogeneous data. Generally the average value lies some where in between the two extremes, i.e. the largest and smallest items. It is calculated as follows:

$$\text{Arithmetic Mean } (\bar{X}) = \frac{x_1 \Gamma x_2 \Gamma x_3 \dots \dots \Gamma x_n}{N}$$

$$\text{Or, } (\bar{X}) = \frac{x}{N}$$

Where,

Σ = Sum of the sized of the items

N = Number of items

ii. Standard Deviation (†)

Karl Pearson first introduced the concept of standard deviation. Standard deviation is the positive square root of the arithmetic average of the square of all the deviation measured from the arithmetic average of the series. The standard deviations measure the absolute dispersion of a distribution. The greater the amount of dispersion the greater the standard deviation, i.e. greater will be the magnitude of the deviation of the values from their mean. A small standard deviation means a high degree of uniformity of the observation as well as homogeneity of a series. It is calculated as follows:

$$= \sqrt{\frac{\sum fX^2 - \frac{(\sum fX)^2}{n}}{n}}$$

iii. Coefficient of variation (C.V.)

It is the measurement of the relative dispersion developed by Karl Pearson. It is used to compare the variability of two or more series. The series with higher coefficient of variation is said to be more variable, less consistent, less uniform, less stable and less homogenous. On the contrary the series with less coefficient of variation is said to be less variable, more consistent, more uniform, more stable and more homogenous. It is denoted by C.V. and is obtained by dividing the standard by arithmetic means. Thus,

$$C.V = \frac{\text{Standard Deviation}}{\text{Mean}} \quad \text{i.e.} \quad C.V. = \frac{\text{Standard Deviation}}{\text{Mean}}$$

F-Statistics

It is the ratio of independent chi-square variates divided by the respective degrees of freedom. The object of F test is to discover whether the two independent estimates of population variance differ significantly, or whether the two samples may be regarded as drawn from the normal populations having same variance.

ANOVA

When we need to test the homogeneity of several means, ANOVA is the powerful statistical tools. It provides a technique to make inferences about whether all the samples have come from the same normal population having the same mean.

Coefficient Correlation

It is the statistical tool that we can use to describe the degree to which one variable is linearly related to another.

CHAPTER-IV

PRESENTATION AND ANALYSIS OF DATA

This chapter is devoted to the presentation, analysis, interpretation and scoring the empirical finding out of the study through definite course of research methodology. To achieve the stated objective of the study and also to make the reader easier to understand the findings qualitative as well as quantitative data and information has been analyzed.

4.1 Leasing Business in Nepal

In this world of financial market, Leasing has also been one of the very good areas of investment. The world today is making steady progress in Leasing Business. Leasing has become increasingly important source of financing during the post world war II era. But in the context of Nepal it is a new concept of the finance companies to finance the organization or an individual to acquire an asset, which can benefit both the users and the financier. This concept of financing method is only about ten years old. Leasing business in Nepal started with operation of finance company named “Union Finance Company” on 21st of Mangshir in 2051 B.S. It was the first step of entering of leasing business in Nepal, done professionally by the finance company. Then other two finance companies named “International leasing and Finance Company” and “Nepal Sri Lanka Merchant Bank” also joined the market of leasing in 2052 B.S. And it was lately the “World Merchant Banking and Finance Company Ltd.” which entered the finance industry doing leasing business also in the mid of the year 2058 B.S. in Hetauda.

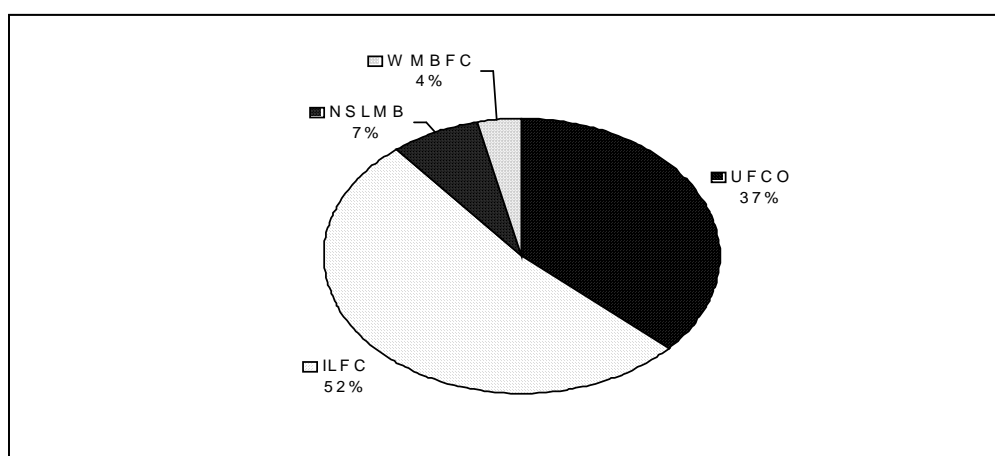
Though we can find both financial and operating lease in Nepal, it is the financial lease that mostly prevails in the market. And this study also focuses mostly on financial lease performed by the finance companies. Till now, no market and regulatory compulsions have yet forced any major move towards operating leases. As there are not any specific rules or acts regarding leasing

business, finance companies are allowed to do leasing business under the Finance Company Act 1986. Beside this, there is not any act that directs the leasing business.

Lease finance outstanding as of mid July 2003 stood at Rs.363.6 million representing 3.02% of the total credit granted by finance companies, which includes Rs.13.3 million from “World Merchant Bank and Finance Company Ltd.”, Hetauda. And rests are from the finance companies of Kathmandu valley that are performing leasing business, in which major portion of around Rs.191.2 million is from ILFC. And the share of UFCO and NSLMB are Rs.133.1 million and Rs.25.8 million respectively. The above discussion is presented in pie chart shown below.

Figure 4.1

Pie Chart showing percentage share of individual finance co.’s (of total Lease Finance in the year 2008, Mid-July)



Sources: NRB’s Non-Bank Financial Statistics No.5 (mid-July 2008)

Figure 4.1 clearly shows that 52 percent of the Lease finance has been done by International Leasing and Finance Company; making company the market leader. Then followed by Union Finance Company covering 37 percent of the total lease finance. The other two finance companies have very marginal share

in the lease finance of only 7 percent by Nepal Sri Lanka Merchant Bank and 2 percent of World Merchant Banking and Finance Company. This clearly shows that there are only two market leaders, and indicates Nepal's infancy stage of the leasing business

4.2 Terms used in the Lease Contract

In this part of the analysis, the terms that are used in the lease contract frequently are described in brief.

Applicable Rate – “Applicable Rate” means a rate of interest defined by the company.

Business Day – “Business Day” means a day when banks of the city of Kathmandu are open for business.

Compulsory Acquisition – “Compulsory Acquisition” means requisition for title or other compulsory acquisition of the equipment (otherwise than by requisition of Lease) capture, seizure, detention for any period exceeding thirty days or confiscation of the equipment by any government or by persons acting or purporting to act on behalf of any government.

Equipment – “Equipment” means the equipment described in the schedule together with all or any parts, equipments and manuals.

Initial Rental – “Initial Rental” means the initial rental specified in the schedule provided to the lessee.

Management Fee – “Management Fee” means the certain amount that is payable to the lessor/finance company by the lessee on signing of the contract (which is usually 1-1.5 percent).

Permitted Lien – “Permitted Lien” means liens or claims for taxes or government charges or levies not yet assessed or if assessed, not yet due and payable or of any repairer, warehouseman, workman or supplier.

Purchase Agreement – “Purchase Agreement” means the agreement, described in schedule provided to the lessee, for the purchase by the lessor of the asset.

Rental – “Rental” means the equal amount of monthly installment payable by the lessee to the lessor as a part of the payment of the lease finance.

Residual Value – “Residual Value” means the price specified in the schedule provided to lessee payable on exercising this option to purchase.

4.3 Clauses of the Lease Contract

This part of the analysis will help the reader understand about the clauses embedded in the lease contract. As the part of the objective is to find out the most important clauses of the lease contract, the clauses are explained in detail to study analyze the importance of the clause.

4.3.1 Acquisition of Asset for Leasing

As per the practice of ILFC, the lessee becomes solely responsible for all the procedures required, for the acquisition of the equipment such as ordering, obtaining approvals for importing, custom clearance etc. The lessee must perform these activities in such a way that the lessor company’s ownership of the equipment is expressed and clear. Within the previously agreed time limit by both the parties, the lessee must complete all the acquiring process. Upon arrival of the equipment, lessee issue and forward to the lessor company a certificate of the equipment acceptance and lease execution certificate. From that date, the lessee is entitled to use the equipment.

As far as the practice of UFCO is concerned, it also appoints the lessee to act as the company's representative for the purpose of acquiring asset. Lessee is required to take all the responsibilities for this entire process and the lessee cannot refuse the asset in any way after its acceptance. The lessee must sign an acceptance certificate. Being the representative, lessee does not acquire any right, title or interest in or to the equipment other than accepted by the company.

NSLMB also makes the lessee responsible as agent of the company for all the matters in connection with the obtaining and use of such equipment. Lessee himself is responsible for any delay and defaults in delivery. The lessee must issue acceptance receipt as expeditiously as practicable and in any case within 12 days after receipt of equipment. After issuing this certificate, the lessee can use the equipment.

4.3.2 Operation of the Equipment

Regarding operation of the equipment, ILFC requires lessee to affix the ownership marking immediately upon taking delivery. The lessee can use asset at the place specified by the agreement but the lessee cannot remove the asset from that place without prior written consent of the company. The lessee must exercise due and reasonable care while using the equipment. He must ensure that equipment is being operated in accordance with applicable manufacturer's instructions and comply with all laws, regulations, ordinance and instructions of any governmental authorities concerning the use, operation and maintenance of the equipment.

The practice of UFCO is also similar to that of the practice of ILFC. As per the practice of UFCO also the lessee must ensure that the equipment is not used in any manner or for any purpose that contravenes any applicable legal provision, any certificate, licenses, or registration relating to the equipment or the insurance or for which it is not designed or suited. Lessee also must insure that

equipment is at all times operated in accordance with the manufacture's approved operating manuals and maintain all licenses certificates and manual that is required for operating equipment.

NSLMB too, does not allow the lessee to use for any purpose for which it is not designed or other wise than in accordance with any operating instruction used by the manufacturer or supplier. The company, instruct the lessee to affix ownership label, plate or other marking on the equipment at the lessee's own cost and not to remove or change such markings. Moreover, NSMB requires the lessee to take all necessary steps to ensure that the equipment is safe and risk free for the health of employees and others. The company remains indemnified at all the times against any claim, which may be made by such employees and others.

4.3.3 Lease Rentals

As defined in the terms of lease contract, it is the equal monthly installment payable to the lessor. The lessee shall pay to the lessor by such method that both parties agree upon from the time specified to the lessee.

It has been found from the study that all the companies take decision for lease term and lease rental on the basis of appraisal of the lessee and his business. For all the companies lease period begins from the date when the lessee issues certificate of lease execution to the lessor. For and in consideration of the lease of the equipment, companies demand lease rental differ from case to case of leasing transactions.

ILFC demand first rental, management fee and commitment fee in cash in the execution date and decide about other rentals on the execution date. In the event the lessee fails to make payment when due to the lessor, charging on such unpaid sum penalizes the lessee.

In the same way, UFCO demand the initial rental and management fee on the execution date and requires other installments without demand of the company punctually as specified by the company. If prior to the execution date the company has paid any amount regarding the purchase of the equipment, the company demands pre-rental on those payments. UFCO gives utmost importance to the time of payment of rental and all other sums whatever due. If any rental or any other amount payable to the company is not paid on the date on which it becomes due, the company charges interest at the default rate.

In the case of NSLMB the lease rental is payable at the end of the month.

This clause mentions specifically about the timely payment of all the due rentals without any demand by the lessor. For the time of payment and the amount of rental the lessor provides a schedule of payment known as loan amortization schedule. This schedule includes all the information about the rentals, principal amount and interest on due amount.

4.3.4 Interest on overdue amounts

If any rental or any other amounts are payable to the lessor under the lease agreement is not paid on due date, the lessor shall be entitled to demand interest on such overdue amounts using default rate as per the rules of the finance company.

This part of the lease contract mentions about the compulsory payment of interest on the overdue rentals to be paid to the lessor. This makes sure that the lessor's receivables are not invested without any interest. And also helps the lessor to get timely payment of the rentals. Interest on overdue amount charge by all the three finance co's are same ie. 1 percent on installment amount.

4.3.5 Residual Value

The residual value is the value of the asset at the end of the lease period. The lessee may purchase the asset at the end of the contract on payment of the residual value, which is the last payment of the schedule.

This part of the lease contract mentions about the value of the asset at the end of the lease contract. It is the book value of the asset at the end of contract and lessee are usually offered with the same amount to purchase the asset.

4.3.6 Exclusion Clause

The lessor doesn't give any warranties and doesn't makes any representatives as to the quality, condition, correspondence with description, or suitability for the lessee's purpose of the equipment. And lessor also doesn't authorize any dealer or supplier for any warranties. All warranties and representations implied by law in respect of the equipment are excluded unless it is prohibited by the statute. The equipment is leased and if applicable is sold on an "as is where is" basis. The owner warrants that it will have and on any sale will pass to the lessee only such title as the lessor may acquire under the purchase agreement.

The purpose of the implication of this clause is to notify the lessee that the lessor doesn't take any responsibilities regarding warranties provided by the supplier. Also the dealer or supplier of the asset is not authorized by the lessor to provide the lessee with any warranty. The warranty for assets is only the agreement between the supplier/dealer and the lessee only.

4.3.7 Warranties of the Leased Asset

At the request and expense of the lessee, the lessor will assign to the lessee the benefit of any guarantee or warranty issued by the manufacturer in respect of the asset if the same is assignable. This clause mentions about the lessor acting

as an intermediary between the lessee and the supplier if the supplier provides any warranty. The lessor however will not provide any warranty for asset leased on its own.

4.3.8 Maintenance and Repair

Maintenance part explains about the maintenance of the leased assets by the lessee where as repair part of this clause explains about the responsibilities of the lessee on the leased asset for its repair in case of any sort of damage.

Regarding repair and maintenance of the equipment, the practice of ILFC has been found that the lessee maintains the equipment in good operating condition and working order as long as he has possession. For the purpose of repairing and maintenance, the lessee can enter into any agreement with any third parties who has been designed by the manufacturer or supplier. The lessee also should comply with all mandatory modifications, service bulletins and similar mandatory requirements applicable to the asset or to any part. The lessee also need to comply with all laws and regulations applicable to the asset for the time being in force and provide the lessor with such evidence as the lessor may require to satisfy that the lessee has complied with the requirements of this clause.

In case of UFCO also, the lessee must keep the equipment in good repaired condition and functioning all respects. All necessary repair and maintenance must be done at lessee's expenses and replacement (if necessary) of the same or greater utility designed or suitable for the equipment. UFCO holds ownership in all substitutions, replacement and renewals made without further act or deed as well as in removed parts until such time as replacement us made. Moreover, UFCO requires lessee to keep the proper records of all maintenance carried out and permit the lessor to examine and take copies of such record at any time upon giving the lessee reasonable prior notice.

NSLBM also makes the lessee fully responsible for maintaining the equipment at the lessee's cost to keep the equipment in working condition. The lessee must give immediate notice to the company about any loss or damage. In case the lessee fails to repair the equipment, the company itself repairs the equipment and reimburses the cost from the lessee. Such loss or damage does not affect the obligations of the lessee. The lease agreement remains in full force and effect.

4.3.9 Lease Deposit or Security

The study has shown that, in order to secure the performance of all the obligations of the lessee, all the companies undertaken in this research require certain deposit or security from the lessee on such deposit or security.

4.3.10 Attachment, Alteration and Transfer of the Equipment

ILFC prohibits the attachment of the equipment to any real state or any other personal property and lessee is not allowed to modify the features, performances and specifications of the equipment without prior written consent of the company. Any modifications even with the company's consent are done at lessee's own responsibility and expenses. If the lessee alters the original state on the equipment with the company's prior written consent all accessories, parts and replacement for or which are added to or become attached thereto becomes the company's property. Regarding the transfer of the equipment, companies prohibit to assign, transfer, pledge, hypothecate or otherwise dispose of the equipment or any part of the equipment to third party.

UFCO does not allow lessee to maintain the operating base for the equipment in any country other than kingdom of Nepal or a country approved by the company. In addition to this provision, lessee does not get permission to do any thing that might jeopardize the company's ownership of the equipment and results in the equipment being arrested, confiscated, sized, impounded or otherwise taken from the possession of the lessee. The company calls for

immediate written notice and promptly procures release there from the equipment.

NSLMB also does not allow, without prior written consent of the company, to affix or otherwise attached the equipment to immovable property, alter, add, and improve the equipment. If the lessee does so, all the parts become the company's property. Moreover, lessee cannot sell, gift, assign, let on hire or otherwise dispose the equipment in any manner.

4.3.11 Indemnities to the Lessor

The lessee shall indemnify and keep the lessor indemnified against all the costs and expenses of purchasing, owning, operating, insuring, maintaining and repairing the asset. If the lessee has failed to do so in accordance with the terms of the agreement, the lessee shall reimburse the lessor for all the expenses explained earlier. The lessee also shall indemnify the lessor for all damages, liabilities, claims and expenses, which may be at any time claimed against the lessor by any agent, sub-contractor of the lessee or by any third party arising out of the purchase, use or ownership of the asset.

This clause is set for the protection of the lessor against the expenses made by itself on behalf of lessee. The lessor has the right to claim all the expenses made for leased assets, which is due to the lessee. The lessor is also protected from the claims of the third party relating to the leased asset and the lessee.

4.3.12 Insurance of the Leased Asset

All the finance companies require the leased assets to be insured at the lessee's expense. The companies themselves determine the amount, coverage and insurer and obtain and maintain insurance policy for the entire period of the lease at the company's name but the lessee pays the premium. The practices found regarding payment of premium are that lessee can directly pay the insurer or can request the lessor to pay the insurance premium on its behalf.

But the option used in ILFC and NSLMB is that the lessee is required to pay the premium through company's account. And such payments made before lease execution are included in the acquisition cost of the asset.

If the insurance is canceled or any material change, which affects the interests of the lessor, the lessee without any injustice to the simplification of the foregoing, the policies shall name the lessor as the owner and warrants no operational interest. The companies also require that at any time, the amount of insurance against loss or damage to the equipment must not be less than the corresponding stipulated loss value after execution date. However, before execution date, the companies themselves in consideration of the stipulated loss value of the first year determine the amount of insurance.

Upon studying the insurance clause of the lease contract, it is found that it is one of the sophisticated clauses in the lease contract. However, it is one of the important clauses of the lease contract, as it covers the risk indulged in any business including the leasing business. As one might know that insurance covers the risk involved in the assets of any type. And it is wise to insure any asset involved, be it for personal use or for business purpose. And for the business purpose, that also for leasing business, insuring the leased asset is the must, as the leased assets can be ruined and it may be difficult for the lessor to get its investment back. So, it can be said that, it helps the lessor to remain safe from the loss that can be occurred due to bad debt (occurred by the damage to the asset and total lost of the asset by fire or theft) by insuring the leased asset with the insurance company. And the lessor has clearly mentioned that the insurance of the leased assets is a must and the amount is payable by the lessee and also any benefits is in the account of lessee (after deducting any amount due).

4.3.13 Default and Remedies

The term default itself refers to the incompetence in performing particular acts and the same is also applied in the lease contract. There are several cases that may cause the lease contract to be deemed as default. The lessor may serve notice terminating the lease, where the lessee shall make all the payments required (as per defined in the payment on termination) and must return the equipment to the lessor if the contract is deemed as default.

In the practice of ILFC, if any of the following events occur and company thinks is unsatisfactory, agreement is deemed to be in default:

-) If the lessee defaults in the performance of any clause of the agreement.
-) If the cheque issued by the lessee dishonor.
-) If the lessee has suspended or closed its business or resolve to dissolve itself.
-) If the lessor determines that lessee's business cannot be continue further.
-) If the lessee filled application for public sale, liquidation, bankruptcy, provisional execution etc.

Likewise UFCO'S practice in connection to the default has been found as follows:

-) If the lessee fails to pay any sum payable under the lease agreement (usually between 5-7 business days) of its becoming due or upon the case of no due date specified in the lease agreement, usually within 5-7 business days after the demand of payment by the lessor.
-) If the lessee is in breach of agreement of lease or any other contracts made between the lessee and the company.
-) If the lessee does any acts which prejudice the company's title or rights in the equipment.

-) If the equipment is arrested, impounded or detained and does not release within 10 business days.
-) If any representation and warranty made by the lessee or any document or information furnished to the company are shown to have been wrong or misleading.
-) If a resolution is passed for the lessee's liquidation.

The practice of NSLMB in this regard seems as follows:

In cases where the lessee fails to pay any due amount within 7 days of its becoming due or fails to perform any of the obligations and if it does such acts which jeopardize the lessor's right in the equipment, the company, by notice may terminate the agreements.

Likewise, if the lessee permits any legal judgment against the equipment, if the lessee becomes bankrupt, if the lessee (in case the lessee is corporate body) goes on liquidation, the agreement is deemed to have been automatically terminated.

So in general the contract is deemed to be default, if the lessee jeopardizes its own business and put the lessor also at risk of losing the investment.

For the remedies or to cover the loss (in case of default), the lessor has the following rights on the lessee and the leased assets:

-) The lessor can without any notice, be entitled to remove and repossess the asset and the lessor will not be responsible for any loss occurred by such deed.
-) The lessor can recover the entire amount due by rentals for the fixed period of lease.
-) The lessor can also recover other amounts (other than rental) that are payable by the lessee had the lease agreement continued.

-) The lessor has the right to sell or dispose off the assets seized under the case of default.
-) In case of total loss of the leased assets, the lessor has the right to demand the compensation agreed beforehand and the amount equal to the rentals due.

The lessor's rights are the strong points that are made totally for the safety of the uses of funds in the lease finance. The rights on the leased assets in case of default serve as the gateway to solve the problems thus arrives. All the clauses are designed to recover all the amount due that the lessor has right on. However, the lessor shall have to pay the lessee any insurance proceeds if received by the lessor (after deducting the amount due by lessee).

4.3.14 Renewal of Lease after Expiry

ILFC renew the lease if the lessee gives written notice to the company no later than two months before the expiry of the lease. In such case the rentals and stipulated loss value for the renewed lease are changed. The term of renewed lease is extended for the period of one year and other terms and conditions remain unchanged.

UFCO generally does not renew the lease for secondary period. On the termination of the lease the lessee return the equipment at the expenses of the lessee to the company at such a location as the company may designate but if the lessee wish to purchase the equipment, he must pay the residual value.

NSLMB also provides the facility of renewing lease. It does not terminate the lease from its part, if it is fully satisfied with the lessee, until terminated by the lessee. Such renewed lease covers same terms and conditions as before expect the lessee pay yearly rental in advance.

4.4 Study of Growth of Leasing Business in Nepal

As we are aware that in this world of financial market, leasing business is also one of the good areas of investment. In fact, very large volumes of business are successfully carried out through leasing operating in advanced countries. But unfortunately in Nepal Leasing Business has not been able to get momentum although it passed a fair length of time.

According to the provision made under section- 3 of Finance Companies Act 1986, finance companies are legally allowed to make available leasing finance to any individual firm, company or institution for the purchase of vehicles, machinery tools, equipment, durable household goods or other similar movable property. Though the finance companies act is enacted in 1986, there is no any finance company established till 1993. It was lately in 2051 B.S. with the establishment of Union Finance Company, the leasing business took its first step. And later other finance companies also started doing leasing business, which is already mentioned in part 2.1. In this part, we are going to discuss about how the leasing business has grown since establishment by analyzing the amounts investment in the leasing business by various finance companies in the past.

As stated earlier leasing business in Nepal started with the establishment of UFCO in 2th of Mangshir 2051 B.S. During the year of first operation, Rs.26.3 million was invested in lease finance by UFCO. And later in the year 2053B.S. International Leasing and Finance Company and Nepal Sri Lanka Merchant Bank also entered in the leasing market. The three finance companies' total investment in the year 2053/54 B.S. stood at Rs.52.5 million. This shows a good indication of probable growth of leasing business in Nepal. And as it indicated the following year showed an astonishing growth in leasing business by doing business of Rs.185.0 million and Rs.310.3 million in the year 2054/55 and 2055/56 B.S. respectively.

This tremendous growth of leasing business suddenly started to slow down and the amount invested in the lease finance started to decline for two consecutive years till 2059/60 B.S., falling down to Rs.235.3 million. But it was not the climax of the leasing business that is going to end miserably, rather the concluding years again found a growth in lease finance moving up to Rs.277.8 million in 2061/62 B.S. and Rs.363.6 million in the year 2062/63 B.S. The investment of the total amount in lease finance in the year 2061/62 B.S. is the highest recorded in the history of leasing business in Nepal. This highest investment includes a nominal contribution of Rs.13.3 million by newcomer World Merchant Banking and Finance Company (WMBFC), in compared to the contribution of Rs.191.2 million by ILFC and Rs.133.1 million by UFCO.

The above analysis is shows in the table 4.2. But unfortunately leasing business in Nepal can't maintain the growth trend. The tremendous growth of leasing business started to slow down in the year 2061/62, falling down to Rs.128.8 million. Similarly in the year 2063/64, was decrease in investment in lease finance ie. falling down to Rs. 138.2 million but in the fiscal year 2064/65 there was a nominal increment in lease finance moving up to Rs.227.2 million

Table no. 4.2
Table showing total amount of fund used in lease finance and its share & growth in percentage.

(Rs. in million)

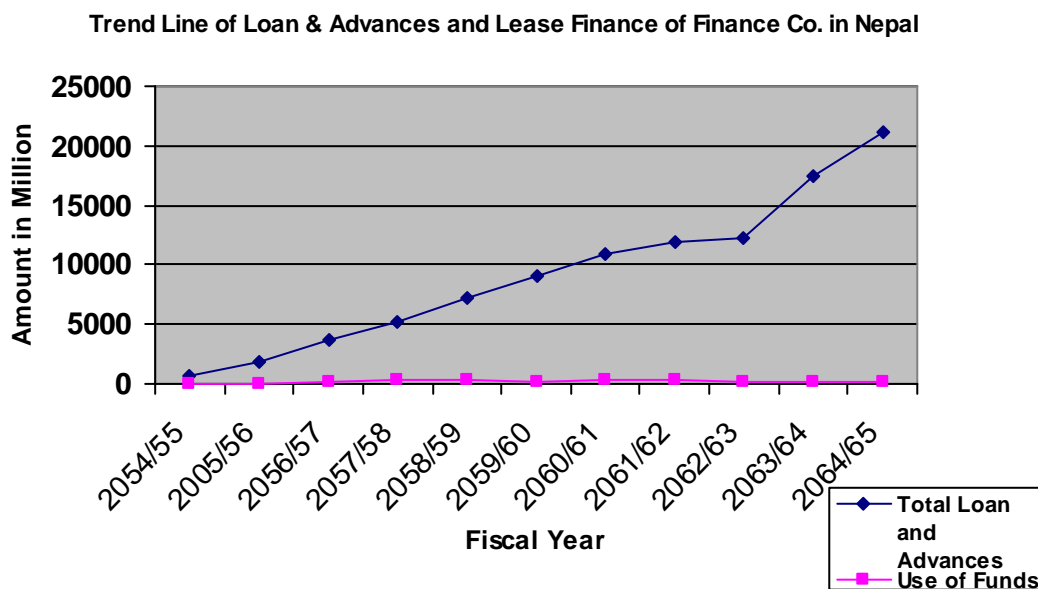
Year (B.S.)	Total Loans and Advances	Uses of funds in Lease Finance	Share of Lease in Percent	Percentage Increase in Lease Finance
2054/55	670.6	26.3	3.92	-
2055/56	1852.9	52.5	2.92	107.22
2056/57	3667.1	185.0	5.02	239.25
2057/58	5277.7	310.3	5.66	67.73
2058/59	7218.8	260.1	3.60	-16.18
2059/60	9062.8	235.3	2.59	-9.53
2060/61	10865.3	277.8	2.56	18.06
2061/62	11929.6	363.6	3.02	30.88
2062/63	12273.7	128.8	1.02	-59.07
2063/64	17520.8	138.2	0.78	-7.12
2064/65	21223.3	227.2	1.16	78

Source: NRB Banking & Financial Statistics No.25

Table 4.2 also shows the share of lease investment in the total loans and advances. If we analyze the “share of lease in percent” column, we can find that the investment of fund in lease is lower in 2061/62 than in the year 2054/55. That is, there has not been proportionate increment in the leasing business in accordance to other investments like loans and advances. We see rather ups and downs in leasing business in compared to the smooth growth of other investment area of finance companies. We can notice from the above table that the share of lease in percent in a fiscal year 2062/63 and 2063/64 are just 1.02 percent and 0.78 percent which clearly shows that the proportion of leasing as compare to Loan and Advance is very low. Therefore lot of activities and home work must be done in order to uplift the percentage of share in leasing in Nepal.

For more clarification Table 4.2 has been presented graphically below:

Figure no: 4.2



4.4.1 Institutional Growth of Leasing Company

In this part of the study, an attempt is made to study and analyze the growth of finance companies performing leasing business. Since, there are no separate act is made for the leasing business, finance companies are allowed to perform

leasing business according to the provision made under section-3 of Finance Company Act 1986 A.D. Although the provision for the lease finance was available since 1986 A.D., the first investment made in lease finance was only in the year 1995 A.D. At that time there existed 3 finance companies performing leasing business. And for the Nepalese lease market it took another seven years to see another finance company performing leasing business. To study the growth and percentage of finance companies performing leasing business with the total finance company, a table has been created for better understanding.

Table 4. 3

Table showing institutional growth of finance companies performing leasing business

Year (B.S.)	Total no. of Finance Co.	Total no. of Finance Co. performing Leasing Business	Growth rate in %	% of Finance Co. Performing Leasing Business
2029	3			
2053	6			
2054	18	1		5.55
2055	35	3	200.00	8.57
2056	39	3		7.69
2057	23	3		6.98
2058	25	3		6.67
2059	26	3		6.52
2060	28	3		6.25
2061	52	2	33.33	7.69
2062	52	2		7.21
2063	57	2		7.02
2064	59	2		6.77
2065	59	2		6.77

Source: NRB Banking & Financial Statistics No.25

From the analysis of table 4.3, we can find that there has been significant growth in the number of finance companies since its establishment. But when we look at the figures of finance companies performing leasing business we see a very low growth. Only in the year 2055 B.S., there has been noticeable growth and rest of the years till 2060 B.S. there was not any growth at all. And after long year one finance company came into existence in the year 2061 B.S. From the last column of the table no. 4.3, it is clear that there are not many finance companies performing leasing business in compared to other financial institutions. The percentage share is very low and has not risen even up to eight percent. This indicates the existence of non-favorable situations in leasing market, which led most of the finance companies to not to invest in leasing business. Those unfavorable situations and conditions are discussed in details in concluding parts.

4.4.2 Extension of Leasing Business around the Country

It is accepted principle that to achieve the balance development of the country, availability of financial services should be extended throughout the country. Therefore, under this research, it has been checked whether the business of leasing has been concentrated in any particular region or spread over the country. To ease the research work, the extension of leasing business has been observed by categorizing the whole country as valley and outside valley. The position has been presented as follows:

Table 4.4**Extension of Leasing Business around the Country**

Year	Total finance companies having leasing business	Companies established in valley	%	Total finance companies performing leasing business established outside the valley	%
1998	3	3	100	-	-
1999	3	3	100	-	-
2000	3	3	100	-	-
2001	3	3	100	-	-
2002	3	3	100	-	-
2003	3	3	100	-	-
2004	3	3	100	-	-
2005	2	3	75	1	25
2006	2	3	75	1	25
2007	2	3	75	1	25
2008	2	3	75	1	25

Source: Banking and Financial Statistics. NRB Vol 25.

Table 4.4 shows that before 2004 all the finance companies operating leasing business were concentrated in valley only. But in the year 2005 one finance company, established outside the valley, has started leasing business. It is the World Merchant Bank established in Hetauda. It indicates that, business of leasing has been just started outside the valley representing the positive steps for the development of leasing business.

4.5 Uses of fund in lease finance by ILFCO, Union Finance & NSLMB

Table 4.5

Uses of funds in Lease Finance by Different Finance Company

(In million)

Year	ILFCO	UFCO	NSLMB	WMBFC	Total lease financing in Nepal
2001	29.29	130.92	129.86	-	310.29
2002	21.2	100.3	118.2	-	260.1
2003	61.1	91.2	83	-	235.3
2004	127.5	86	62.3	-	277.8
2005	191.2	133.1	25.8	13.3	363.6
2006	115	0	28.6	5.2	128.8
2007	92.6	0	21.6	2	138.2
2008	136.2	70.2	20.7	0.1	227.2
Mean	102.08	76.29	66.53	5.15	
S.D.	27.59	28.25	37.68	5.02	
CV	26.63	63.32	56.62	97.86	
%					

Source: Annual Report of ILFCO, Union Finance & NSLMB

During the study period, in the fiscal year 2005, there was a highest investment in lease finance in Nepal i.e. 363 million. On that part ILFCO contribute 191.2 million, Union finance contribute 133.1 million, NSLMB contribute 25.8 million & WMBFCO contribute 13.3 million. Coincidentally in that year ILFCO, Union Finance & WMBFCO invest highest amount of their fund in lease finance where as NSLMB invest highest amount of 129.86 million of fund in lease finance on 1998 AD.

The above table also reveals that in an average, ILFCO has the highest mean i.e. Among four finance Co. ILFCO invest more amount of fund in Lease Finance. Similarly WMBFCO invest lowest amount of fund on it whereas Union finance & NSLMB invest in between.

The coefficient of variation of WMBFCO is highest among all. That shows the investment in lease finance of WMBFCO is the least consistent while CV of ILFCO is lowest i.e. 26.63 percent. It predicates that the investment of ILFCO is the most consistent among four Finance CO. Similarly Union Finance Co's CV on lease finance is 63.32 & NSLMB CV on Lease finance is 56.62 which indicate that there is more fluctuation in Lease finance of Union finance in compare to NSLMB.

For more clarification the above table is presented in graphical figure below.

Figure 4.3
Investment Trend of Leasing Business

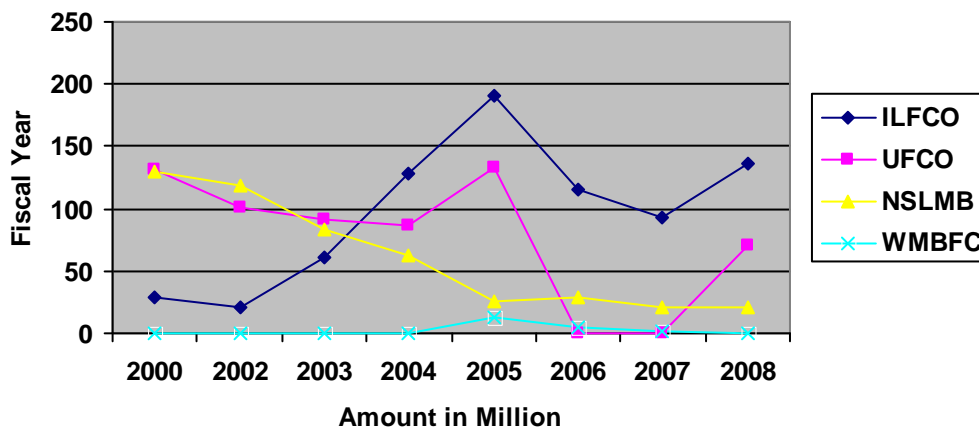


Table 4.6

Segregation of Lease Finance of International Leasing & Finance Co.

(In million)

Year	Vehicles	Tools & Equipment	Durable home appliances & other assets	Total lease financing
2004	112.2	15.3	-	127.5
2005	169.2	21.9	-	191.2
2006	102.3	12.7	-	115
2007	82.5	10	-	92.5
2008	136.2	0	-	136.2
Mean	120.92	11.98	-	132.92
S.D.	29.23	7.17	-	
CV %	22	59.88	-	

Source: Annual Report of ILFCO

Table 4.6 reveals that ILFCO invest more of their lease finance on Vehicles Lease as mean of Vehicles Lease i.e. 120.92 is much more than Tools & Equipment Lease i.e. 7.17. Similarly the coefficient of variation of Vehicles Lease of ILFCO is lower than Tools & Equipment ie $22 < 59.88$. That shows the investment in Vehicles lease finance is more consistent than Tools & Equipment.

For more clarification the table 4.6 is graphically presented below:

Figure 4. 4

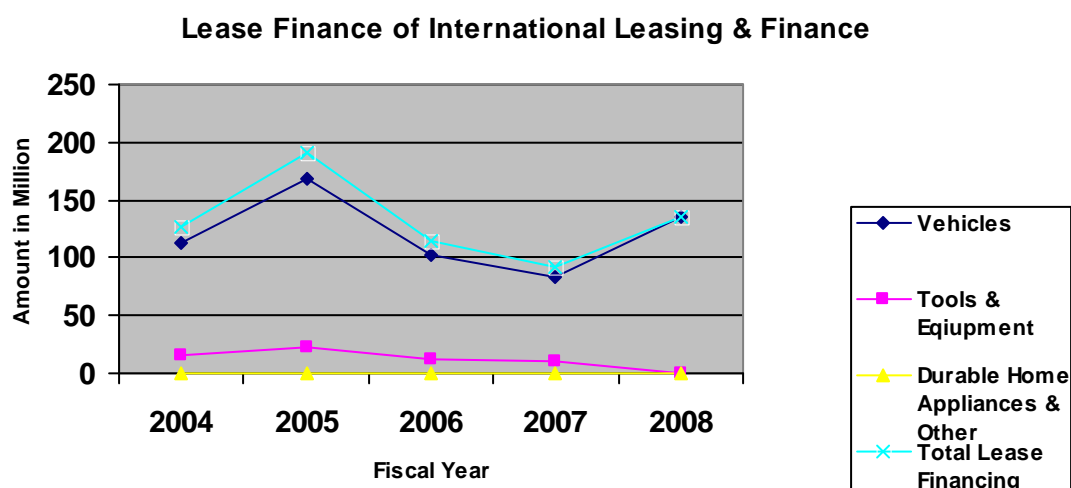


Table 4.7

Segregation of Lease Finance of Union Finance Co.

(In million)

Year	Vehicles	Tools & Equipment	Durable home appliances & other assets	Total lease financing
2004	32.5	53.5	-	86
2005	79.8	53.73	-	133.1
2006	0	0	-	0
2007	0	0	-	0
2008	23.5	26.8	-	70.2
Mean	27.16	30.806	-	73.19
S.D.	29.28	56.56	-	
CV %	107.82	183	-	

Source: Annual Report of Union Finance

Table 4.76 reveals that Union Finance Co. invest more of their lease finance on Tools & Equipment as mean of Tools & Equipment Lease ie. 30.806 is more than Vehicles Lease ie. 7.17. But the coefficient of variation of Tools & Equipment Lease of Union Finance Co is more than Vehicles Lease ie $183 > 107.82$. That shows the investment in Vehicles lease finance is more consistent than Tools & Equipment.

For more clarification Table 4.7 presents the data graphically

Figure 4.5

Lease Finance of Union Finance

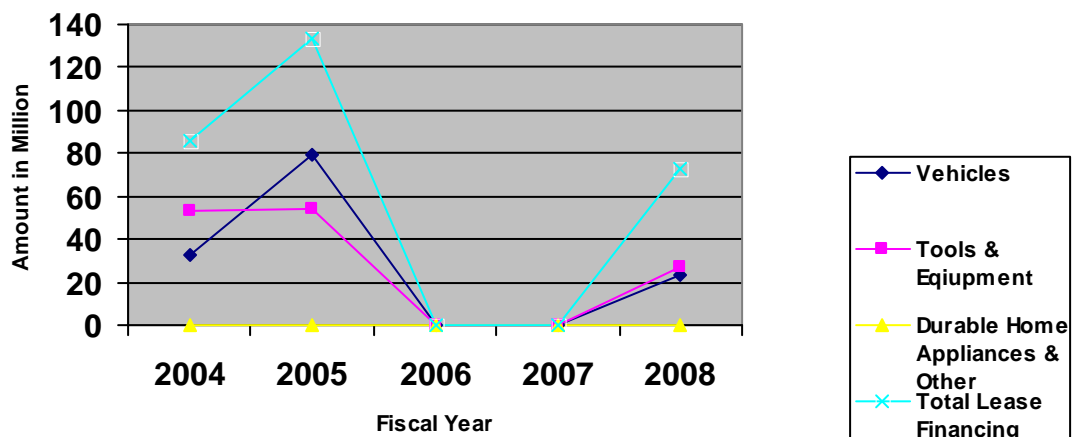


Table 4.8**Segregation of Lease Finance of Nepal Srilanka Merchant Bank.**

(In million)

Year	Vehicles	Tools & Equipment	Durable home appliances & other assets	Total lease financing of NSLMB
2004	57.87	6.23	-	62.3
2005	22.95	2.85	-	25.8
2006	26.2	2.20	-	28.6
2007	38.22	3.23	0.019	21.6
2008	37.26	3.50	0.02	20.7
Mean	36.52	3.682		66.53
S.D.	12.25	1.2229		
CV %	33.53	38.62		

Source: Annual Report of NSLMB

Note: Mean, SD & CV of durable home appliances & other assets are not calculated because data are not sufficient for analysis.

Table 4.8 reveals that NSLMB invest more of their lease finance on vehicles lease as mean of vehicles lease ie. 36.52 is much more than tools and equipment Lease ie. 3.682. Similarly the coefficient of variation of Vehicles Lease of ILFCO is lower than tools and equipment i.e. $33.53 < 38.62$. That shows the investment in vehicles lease finance is more consistent than tools and equipment.

For more clarification the table 4.8 is graphically presented below

Figure 4.6
Lease Finance of Neol Shrilankan Merchant Bank

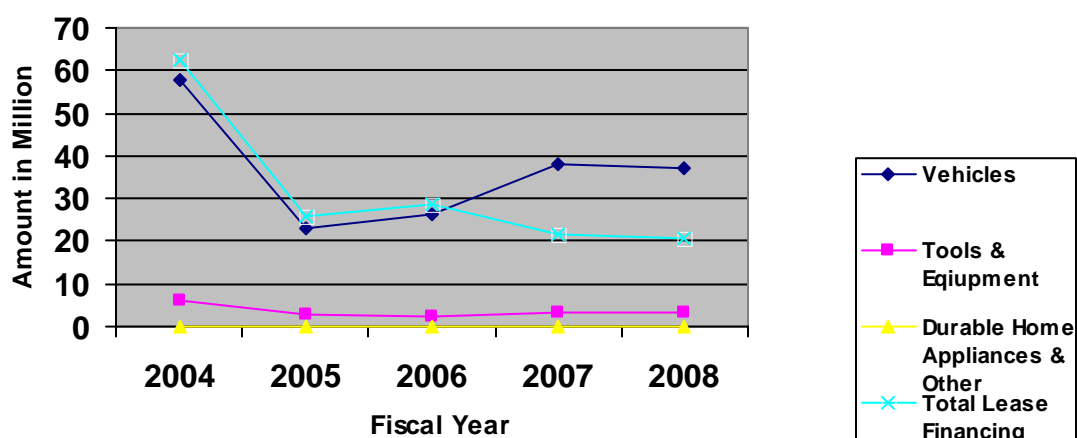


Table 4.9
Lease Financing In Vehicles by Different Finance Companies

(In million)

Year	ILFCO	UFCO	NSLMB	Total lease financing in Vehicles
2004	112.2	32.5	57.87	202.57
2005	169.2	79.8	22.95	272.15
2006	102.3	0	26.2	128.5
2007	82.5	0	38.22	122.92
2008	136.2	23.5	37.26	196.96
Mean	120.92	27.16	36.52	
S.D.	29.23	29.28	12.25	
C.V.	22	107.82	33.53	

Table 4.9 reveals that in an average, ILFCO has the highest mean ie. among three finance Co. ILFCO invest more amount of fund in vehicles lease finance in Nepal. Similarly Union Finance invest lowest amount of fund since its mean is the lowest among three finance co. whereas NSLMB invest second highest

The coefficient of variation of ILFCO is lowest among all ie. 22 percent. That shows the investment in vehicles lease finance of ILFCO is the more consistent while CV of Union Finance on vehicles lease is highest ie 107.82 percent. It predicates that the investment of Union Finance is the least consistent among three Finance Co. Similarly NSLMB CV is 33.53 which can also be considered as consistent.

For more clarification Table 4.9 is presented in graphical figure below.

Figure 4. 7
Lease Finance in Vehicles in Nepal

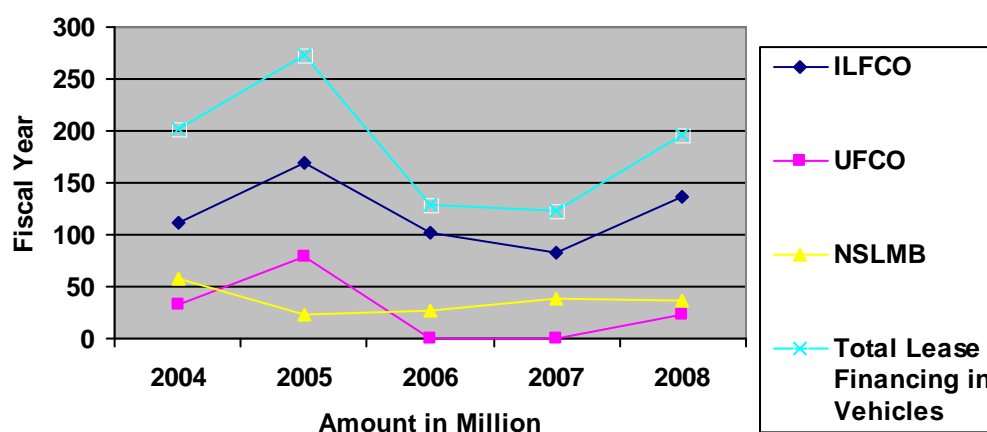


Table 4.10

Lease Financing In Tools & Equipment by Different Finance Companies

(In million)

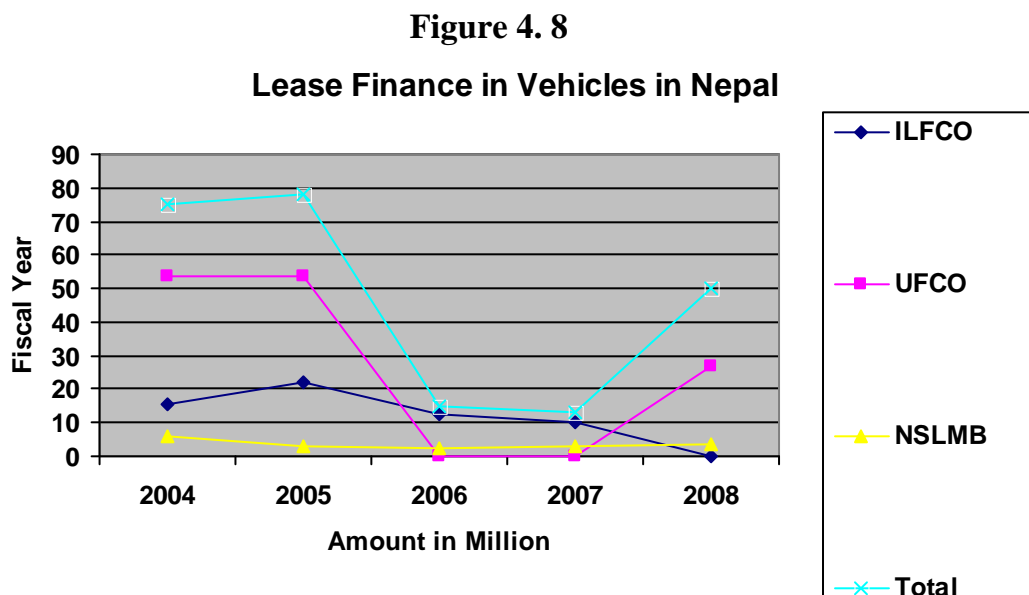
Year	ILFCO	UFCO	NSLMB	Total lease financing in Tools & Equipments
2004	15.3	53.5	6.23	75.23
2005	21.9	53.73	2.85	78.28
2006	12.7	0	2.20	15.1
2007	10	0	3.23	13.23
2008	0	26.8	3.50	50.3
Mean	11.98	30.806	3.682	
S.D.	7.17	56.56	1.2229	
C.V.	59.88	183	38.62	

Source: Annual Report of ILFCO, Union Finance Co & NSLMB

Table 4.10 reveals that in an average, Union finance has the highest mean i.e. among three finance Co. Union Finance invest more amount of fund in tools and equipment lease finance. Similarly NSLMB invest lowest amount of fund since its mean is lowest among three finance co. ILFCO invest second highest i.e. between two.

The coefficient of variation of NSLMB is lowest among all i.e. 38.62%. That shows the investment in tools and equipment lease finance of NSLMB is the more consistent while CV of Union Finance on tools and equipment lease is highest ie 183% It predicates that the investment of Union Finance is the least consistent among three Finance Co. Similarly CV of ILFCO is 59.88 which show average fluctuation.

For more clarification Table 4.10 is presented in graphical figure below.



4.6 Hypothesis Testing

Hypothesis Test and Analysis of Variance of Finance Co. performing Leasing Business.

Hypothesis Test of percent lease finance from loan and advances of three finance companies.

Formulation of Hypothesis

Null hypothesis, H_0 : $\mu_1 = \mu_2 = \mu_3$. That is, there is no significance difference in the % of Lease Finance of three finance companies from their loan and advances.

Alternative hypothesis, H_1 : $\mu_1 \neq \mu_2 \neq \mu_3$ (Two tailed test). That is, there is significant difference between in the percent of Lease Finance of three Finance Co. from their loan and advances.

Table 4.11

One – way ANOVA table

Source of variation	Sum of squares (S.S)	d. f.	Mean sum of squares (M.S.S)	F – ratio
Between Components	SSC = 521	$K - 1$ $= 3 - 1$ $= 2$	$MSC = \frac{SSC}{K - 1}$ $= \frac{521}{2}$ $= 260.5$	$F = \frac{MSC}{MSE}$
Within Components	SSE = 2022	$n - k$ $= 15 - 3$ $= 12$	$MSE = \frac{SSE}{n - k}$ $= 2022/12$ $= 168.66$	$= \frac{260.5}{168.66}$ $= 1.52$
Total	SST = 2525	$n - 1$ $= 15 - 1$ $= 12$		

For details of calculation refer to appendix 02

Level of Significance = 5 %

Calculated F (2, 12) = 1.52

Tabulated $F_{0.05}(2, 12) = 3.89$

Since the calculated value of F is less than the tabulated value of F, it is not significant and H_0 is accepted which means that, the mean of lease finance from loan and advances of sample finance companies do not differ significantly

among themselves. In other words the mean value of percentage of lease finance from loan and advances of population from which the samples have come same. Since it is no significant there is homogeneity in mean value of lease finance (percent of Lease finance of three Finance Co.) from their loan and advances.

Hypothesis Test of Share of Lease Finance from Total Lease Finance

Formulation of Hypothesis

Null hypothesis, H_0 : $\mu_1 = \mu_2 = \mu_3$. That is, there is no significance difference in the share of Lease Finance of three Finance Co. from total lease finance.

Alternative hypothesis, H_1 : $\mu_1 \neq \mu_2 \neq \mu_3$ (Two tailed test). That is, there is significant difference between in the share of Lease Finance of three Finance Co. from total lease finance.

Table 4.12

One – Way ANOVA Table

Source of variation	Sum of squares (S.S)	d. f.	Mean sum of squares (M.S.S)	F – ratio
Between Components	SSC = 5531.579	K – 1 = 3 – 1 = 2	MSC = $\frac{SSC}{K - 1}$ = $\frac{5531.579}{2}$ = 2765.78	F = $\frac{MSC}{MSE}$
Within Components	SSE = 2205.362	n – k = 15 – 3 = 12	MSE = $\frac{SSE}{n - k}$ = $\frac{2205.362}{12}$ = 183.780	$\frac{2765.78}{183.780}$ = 15.02
Total	SST = 7736.921	n – 1 = 15 – 1 = 12		

For details of calculation refer to appendix 02

Level of significance = 5%

Calculated $F_{0.05}(2, 12) = 15.02$

Tabulated $F_{0.05}(2, 12) = 3.89$

Since the calculated value of F is greater than the tabulated value of F, it is significant, H_0 is rejected & H_1 is accepted which means that, the share of Lease finance of sample companies from total lease differ significantly among themselves. In other words, the mean value of Share of Lease Finance of population from which the samples have come is not the same. Since it is significant, there is no homogeneity in mean value of share of Lease Finance between sample finance companies. The reason behind this result is due to the significantly high mean value of ILFCO on the share of lease finance from Total Lease. And also due to the nil investment in lease finance by Union Finance in a fiscal year 2004/05 and 2005/06

Hypothesis Test of Share of Vehicles Lease Finance

Formulation of Hypothesis

Null hypothesis, $H_0: \mu_1 = \mu_2 = \mu_3$. That is, there is no significance difference in the Share of Vehicles Lease Finance of three Finance Co...

Alternative hypothesis, $H_1: \mu_1 \neq \mu_2 \neq \mu_3$ (Two tailed test) . That is, there is significant difference between in the Share of Vehicles Lease of three Finance Co.

Table 4.13

One – Way ANOVA Table

Source of variation	Sum of squares (S.S)	d. f.	Mean sum of squares (M.S.S)	F – ratio
Between Components	SSC = 8763.382	K – 1 = 3 – 1 = 2	MSC = $\frac{SSC}{K - 1}$ = $\frac{8763.382}{2}$ = 2381.692	F = $\frac{MSC}{MSE}$
Within Components	SSE = 1251.95	n – k = 15 – 3 = 12	MSE = $\frac{SSE}{n - k}$ = 1251.95/12 = 102	$\frac{2381.69}{102}$ = 22.13
Total	SST = 10015.332	n – 1 = 15-1 = 12		

For details of calculation refer to appendix 02

Level of significance = 5%

Calculated $F_{0.05} (2, 12) = 22.13$

Tabulated $F_{0.05} (2, 12) = 3.89$

Since the calculated value of F is greater than the tabulated value of F, it is significant, H_0 is rejected & H_1 is accepted which means that, the share of Vehicles Lease finance of sample companies differ significantly among themselves. In other words, the mean value of the Share of Vehicles Lease Finance of population from which the samples have come is not the same. Since it is significant, there is no homogeneity in mean value of the share of Vehicles Lease Finance between sample finance companies.

The reason behind this result is due to the huge variation in the high mean value three finance. And also due to the nil investment in vehicles lease finance by Union Finance in a fiscal year 2005/06 and 2006/07.

Hypothesis Test of Share of Tools & Equipment Lease Finance

Formulation of Hypothesis

Null hypothesis, H_0 : $\mu_1 = \mu_2 = \mu_3$. That is, there is no significance difference in the Share of Tools and Equipment Lease Finance of three Finance Co.

Alternative hypothesis, H_1 : $\mu_1 \neq \mu_2 \neq \mu_3$ (Two tailed test). That is, there is significant difference between in the Share of Tools and Equipment Lease of three Finance Co.

Table 4.14

One – Way ANOVA Table

Source of variation	Sum of squares (S.S)	d. f.	Mean sum of squares (M.S.S)	F – ratio
Between Components	SSC = 3509.77	K – 1 = 3 – 1 = 2	MSC = $\frac{SSC}{K - 1}$ = $\frac{3509.77}{2}$ = 1752.885	F = $\frac{MSC}{MSE}$
Within Components	SSE = 13182.27	n – k = 15 – 3 = 12	MSE = $\frac{SSE}{n - k}$ = 13182.27/12 = 1098.70	$\frac{1752.88}{1098.70}$ = 1.59
Total	SST = 16692.22	n – 1 = 15-1 = 12		

For details of calculation refer to appendix 02

Level of significance = 5%

Calculated $F_{0.05} (2, 12) = 1.59$

Tabulated $F_{0.05} (2, 12) = 3.89$

Since the calculated value of F is less than the tabulated value of F , it is not significant and H_0 is accepted which means that, the mean of Tools and Equipment Lease Finance of sample finance companies do not differ significantly among themselves. In other words the mean value of Tools and Equipment Lease finance of population from which the samples have come is same. Since it is no significant there is homogeneity in mean value of Tools and Equipment Lease Finance.

4.7 Lease Rental Calculation Practiced by Finance Companies

Lease rental is the amount paid by the lessee to the lessor in installments for providing the lease finance service by the lessor. The practice followed by the finance companies regarding payment of Lease Rental is monthly and the depreciation is charged on diminishing balance method. The interest rate charge for the amount of lease varies from one finance company to other finance companies and also within the company it varies from customer to customer. Usually the regular and prime customer gets the privilege of lower interest rates and the new and juvenile are usually charged normal interest rates.

As the practices followed by the finance companies for calculating the lease rental is different from one another, the researcher has tried to present and analyze the calculation of lease rental for each finance company separately.

4.7.1 Practice followed by Union Finance Company

The UFCO has the practice of calculating Lease Rental using the programme called Excel, produced by world-renowned company Microsoft. It does not use any specific software for calculating the lease rental. Neither does it uses any formulae found in the books of finance.

The lease rental is calculated using simple spreadsheet produced by the Microsoft, known as Microsoft Excel. The company defines the amount of assets and then calculates the amount of down payment. The down payment is treated as major rental and placed in the amortization schedule in first place as a part of the monthly rentals. Then the company hypothesize the amount of rental and then uses IRR function available in the excel to find the interest rate (monthly and yearly) using the entire monthly rental including the major rental (here the major rental is treated as expense and is kept in negative figure). Then the excel finds out the rate of return or the interest rate for the hypothesized monthly rental. Then the company uses another function of the excel called “Goal Seek” (found in the sub-menu of the “Tools” in the tool bar) to change the interest rate obtained to the desired one. When the obtained rate is changed using “Goal Seek” function, the hypothesized rental then changes automatically to the required rental as needed (as per the interest rate applied in the cell where interest rate of hypothesized rentals was calculated). And thus the Union Finance Company obtains the monthly lease rental. (The residual value is kept Nil while calculating the lease rentals)

This shows that the UFCO doesn't uses any financial formulae found in the books of finance; rather it uses the modern technology, which is faster and much easier to operate.

UFCO charges certain percentage as management fee (usually 1 percent of lease facility for the old and good clients and 1.5 percent for the new customers) for providing lease finance. The lessee is required to pay certain percentage of the lease facility as down payment at the start of the contract and the required amount for down payment is usually 20 percent-30 percent (depends upon the discretion of the company, it is found that up to 60 percent was also taken as down payment). The amount paid as the down payment is taken as a major rental and is treated as other normal monthly rental, i.e. the amount paid as down payment includes the margin/interest and the amount of principal to be deducted from the total cost of the asset.

A hypothetical example is taken to better understand the treatment of the major rental.

Let, the cost of the Asset be Rs.3, 950,000 “CP”

The down payment is 30 percent of the cost i.e. Rs.1, 185,000 “DP”

The interest rate applied is 16 percent annually (1.33 percent monthly/periodically “PR”)

The contract period is 3 years (36 months/periods)

The down payment of Rs.1, 185,000 is taken as first and major rental. This includes the amount of Rs.36, 862 [(CP-DP) X PR] as interest/margin and the rest i.e. Rs.1, 128,136 (DP – Margin) is the principal amount that is deducted from the cost of the asset to find out the outstanding amount of principal. The equal monthly rental calculated for this example using Microsoft excel is Rs.99, 376.

4.7.2 Practice followed by the Nepal Sri Lanka Merchant Bank

NSLMB also uses Microsoft Excel to find out the equal monthly rental. But it uses and additional the software introduced by Merchant Bank of Sri Lanka to calculate monthly rental unlike UFCO and ILFC. The software comes as a package to calculate lease rental, for which the Merchant Bank of Sri Lanka has their own sets of formula, which was not disclosed by NSLMB for the privacy purpose. The software is relatively much easier to use than used by the UFCO, as it is only required to fill up the predefined cells with the information required to calculate the equal monthly rentals. Once the user enters the amount of the lease facility, lease period (in months), effective interest rate the software automatically calculates the rentals. For the privacy purpose NSLMB did not wanted to disclose the details of formulae involved in the software.

NSLMB, while calculating the lease rental, first deducts the down payment from the cost of the asset. Only after the deduction of the down payment, the actual lease rental calculation is made and also the amortization schedule for the equal monthly rental payment. The amount taken as down payment is not treated as the part of the lease payment, rather as the security for the lease contract. The whole amount received in down payment goes straight in the bank's account. This makes the lease contract of the NSLMB is very much similar to the hire purchase. Where, only the outstanding principal after deducting down payment is treated as finance and the treatment is also made only for the principal outstanding at the beginning of the contract. For example, let the cost of the asset be Rs.100 and the down payment is Rs.30 (30 percent of the cost of the asset), then Rs.70 is the outstanding principal and Rs.70 is taken as loan and the equal monthly payment is calculated for Rs.70 only. While in the pure lease the whole cost of the asset is taken as loan granted and every amount received is the rental, which includes margin and depreciation, which is generally understood as interest and principal.

This kind of practice may be prevailing in this country due to unavailability of separate act for the lease financing which will guide step by step to do the lease financing.

4.7.3 Practice followed by International Leasing and Finance Co.

The ILFC also uses computer software to calculate the lease rental and to prepare the schedule of payment. The software is the same software as used by its other foreign partners in Korea. The software is simple to use as the required monthly rental is easily obtained once all the required data are input. Due to their policy of not disclosing the details on monthly lease rental calculation, the researcher was unable to gather any information or the formulae about the lease rental calculation.

The lessee is required to make a down payment (may vary from client to client) as a deposit in ILFC, which is termed as Key Money. As UFCO and NSLMB, ILFC also charges some percentage of the cost of the leased asset as management fee (which is around 1-1.5 percent). Then the whole of the asset is financed and the lease rental is calculated. For example, let the cost of the asset be Rs.100. Then the amount required to be deposited be 10% (varies from client to client) i.e., Rs.10. ILFC does not deduct this amount or the key money from the cost of the leased asset. The whole cost of the asset (Rs.100) is taken for the calculation of the lease rental. If 12 percent annual interest rate and 3 years (36 periods/months) is applied to calculate the monthly lease rental for Rs.100, then the software of the ILFC calculates lease rental as Rs.3.3783.

The lease rental is payable in advance. The lessee is required to return the asset to the company after the expiration of the contract. The key money or the deposit will be returned to the lessee after the expiry of the contract. However, the lessee is given an option to purchase the leased asset at the predetermined price or to renew the lease agreement on year-to-year basis.

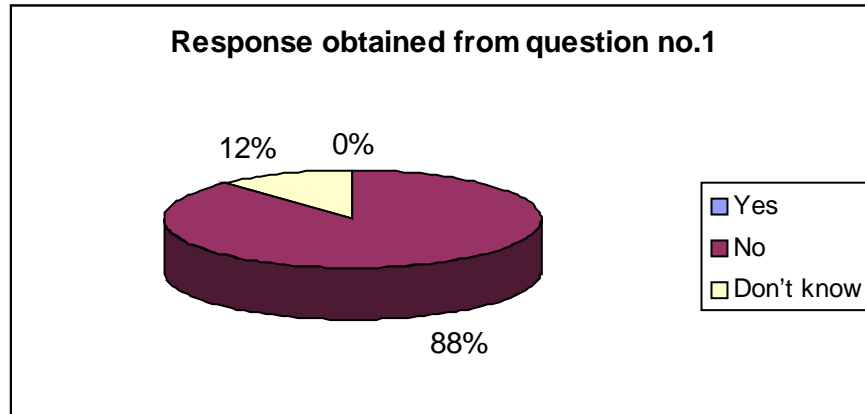
4.8 Primary Data Analysis

During the research study process a series of questionnaire was prepared and pooled the opinion from executives of the selected financial companies. Here is a brief analysis of the respondents' opinions.

Existing Infrastructure for Leasing Business

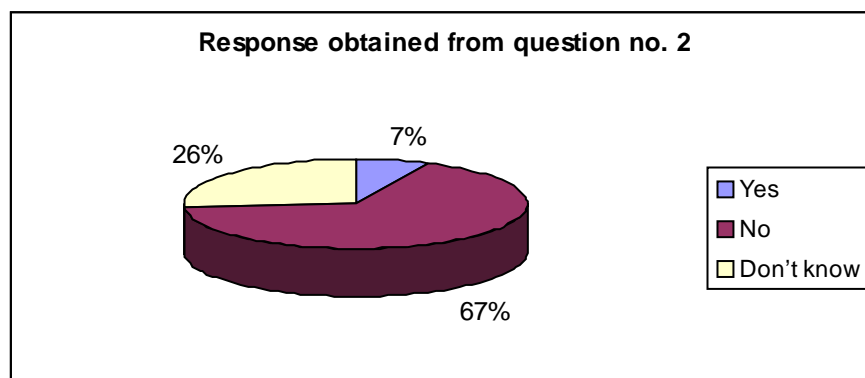
Without necessary infrastructure, no business can be developed. Considering the fact, it has been identified under this research that whether the finance companies are assured to be sufficient infrastructure for leasing business or not. For this purpose, they were asked to specify whether they think existing infrastructure for leasing business is sufficient. Option were provided as 'yes', 'no' and 'don't know'. The result shows that none of the finance companies are confident that the existing infrastructure for leasing business is sufficient.

Among the finance companies 12 percent (2 out of 32) have expressed their views to be unknown to the fact. (For Detail refer Appendix 02 of response obtain from question no.1)



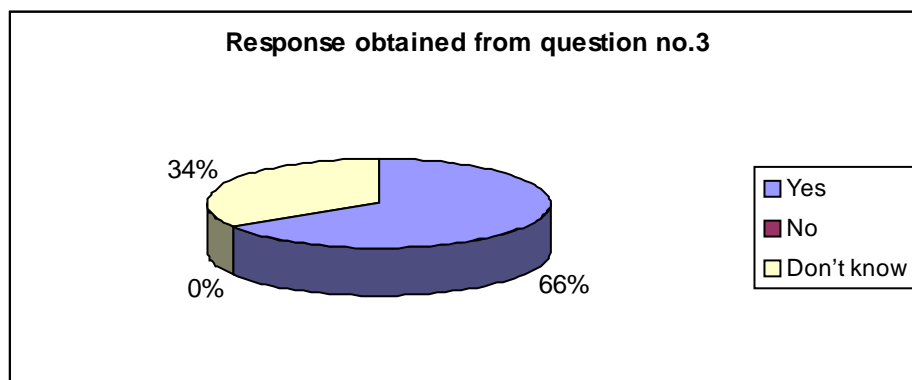
Readiness of Finance Companies for Entering Into Leasing Business

In order to identify, whether the finance companies are ready to enter into leasing industry, these companies are asked whether the present time is appropriate to start leasing business. Referring to Appendix 02 of response obtains from question no.2) – it is found that only 7 percent (2 out of 27) of the finance companies are in view that present time is appropriate to start leasing business. 67 percent of total finance companies are in view that it is not the appropriate time to enter into leasing industry and 26 percent (7 out of 27) are found unknown to the fact.



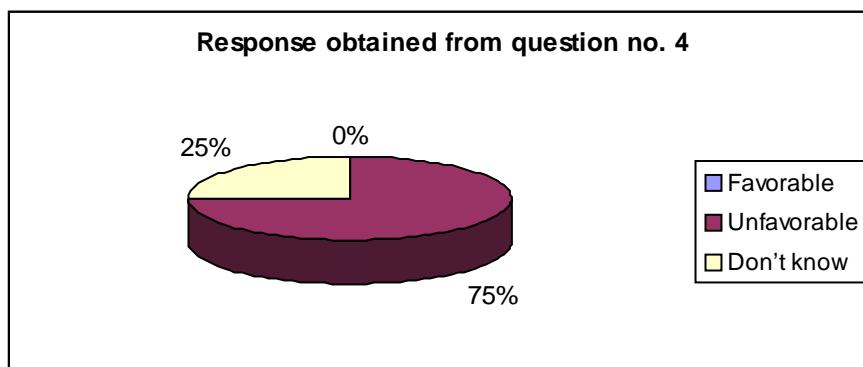
Realization of need to develop Operating Leasing

In order to find whether the finance companies have realized the need of operating leasing in addition to the financial lease, their views have been collected. Referring to Appendix 02 of response obtain from question no.3, it is found that 66 percent (21 out of 32) finance companies opined that there is the need to develop operating leasing in the country. None of the finance companies have opined against it. 32 percent (11 out of 32) of the finance companies have opined that they do not have knowledge about operating leasing. It indicates that majority of the finance companies have realized the need of operating leasing in addition to finance lease. Though the important pie of the finance companies is unknown about the need of operating lease, none of the finance companies have realized that operating lease is not necessary.



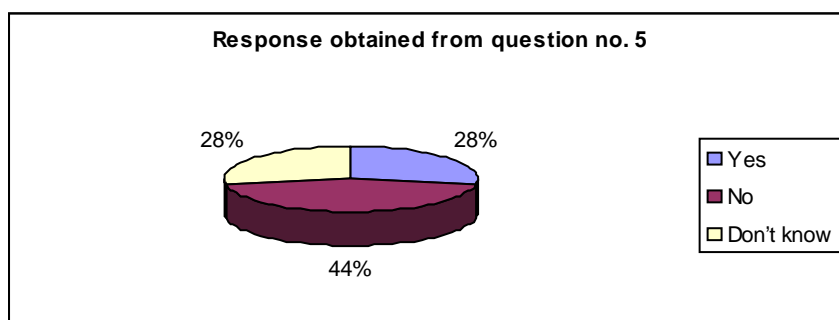
Current Income Tax Act in respect of Leasing Business

Tax concession provided by the income tax plays most important role for the leasing business. Under this research finance companies are surveyed so as to know their view whether the act is favorable for leasing business or not. Referring to Appendix 02 of response obtain from question no.2, it is known that 75 percent (22 out of 32) of the finance companies think that current income tax act is not favorable for leasing business. Other 25 percent (8 out of 32) of the finance companies do not have knowledge about it. None of the finance co. has agreed that current income tax act is favorable for leasing business.



Nepal Rastra Bank’s vision of Leasing Business.

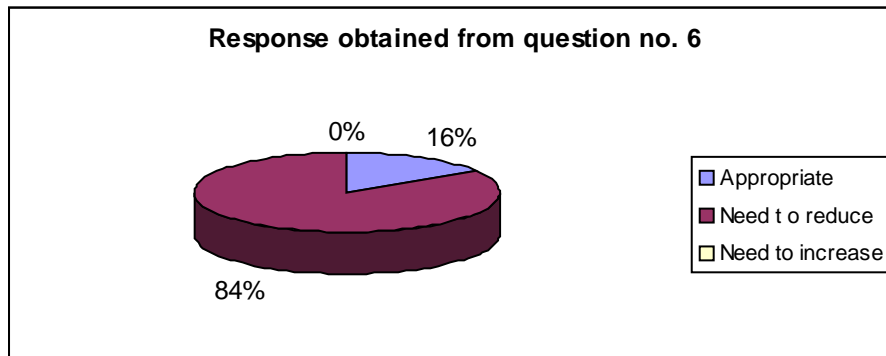
Referring to Appendix07 of response obtain from question no.5, it is known that 22 percent (12 out of 32) of the finance companies thinks that NRB has not yet made clear vision about leasing business and actively creating conducive environment to promote the business. Similarly, 28 percent (9 out of 32) of the finance companies advocate that NRB has a clear vision and is creating conducive environment from its part. Again same 28 percent of the total finance companies are found unknown to the matter.



Appropriateness of Recent Notice of NRB regarding Leasing Business

Referring to Appendix 02 of response obtain from question no.6, it is found that 82 percent (27 out of 32) of the finance companies think that the provision which need 25 crore paid up capital to be maintained in order to carry leasing business in addition to other function is need to be reduced. At the same time, 16 percent (5 out of 32) of the finance companies think that this provision is

appropriate. None of the finance companies thin that this level of capital requirement needs not to be increased.



Obstacles the Finance Co faces in Leasing Business

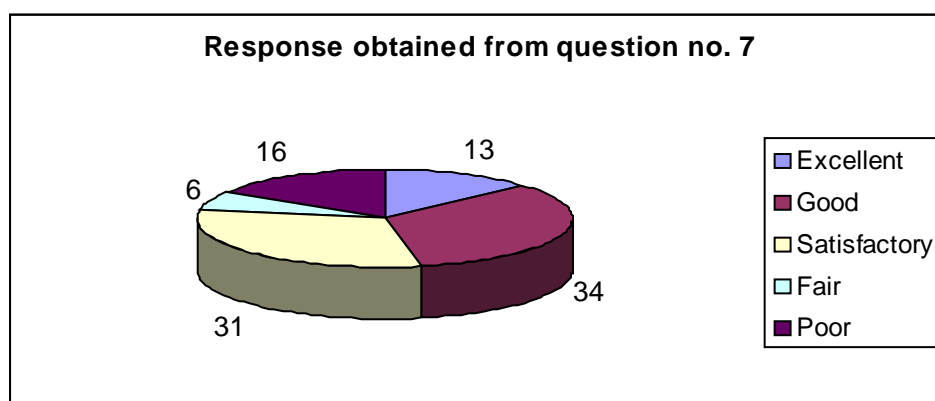
Referring to Appendix 02 of response obtain from question no 7, it is found that the major problem the finance co's faces in leasing business is the absent of lease act. Similarly the next problem is high credit risk. Like wise lack of market is the next problem followed by lack of capital and management problem.

Determinants of Successful Leasing Business

In order to identify the important factors needed for successful leasing business, finance companies were asked to rank the factors that will determine the success of leasing business in future. As show in Appendix of response obtain from question no 8, the credit assessment expertise is in highest priority, speed in utilization of fund isn in second priority and likewise access to cheap source of fund, searching new market and flexibility in lease operation come in third, fourth and fifth priority.

Future Prospect of Leasing Business

Under this research, finance companies assessment of the prospect leasing business in Nepal has been studied. Appendix 02 of response obtains from question no 9, shows that 13 percent (2 out of 32) finance companies have evaluated the future prospect of leasing as excellent. Similarly 32 percent (11 out of 32) finance companies have evaluated as good. In a like manner 31 percent (10 out of 32),6 percent (2 out of 32) and 16 percent (5 out of 32) finance companies have evaluated the prospect of leasing business as satisfactory, fair and poor respectively. It indicates to the fact that there is the largest pie of finance companies that have evaluated the prospect of leasing business as a good. It is also revealed that 78 percent finance companies evaluation is above satisfactory level.



Activities to Be Done To Ensure Bright Prospect of Leasing Business

Finance companies were asked to rank the necessary actions to be done to ensure the bright prospect of leasing business on the base of priority on which those actions are to be done. Referring to Appendix o2 - of Response obtain from question no. 10, it is found that the first activity to be done is- provide clear legal framework regarding the leasing business. Next activity to be done is to increase the effort for publicity of the benefit of this business. Likewise activities prioritized in third; fourth and fifth include provision of tax and other

incentive, development of skilled manpower and increasing effectiveness of practice presently followed by companies.

4.9 Strength of Leasing Business

Without proper and timely reformation, financial sector cannot take full speed on its development process. Nepal has adopted open, liberal and market oriented economic policy since late 1980's and simultaneously financial sector reform programmers have been initiated. But with the passage of time, financial sector is becoming more exciting, challenging and ever-changing sector due to increased economic liberalization and globalization.

To cope with such complex situation, financial innovation should be given priority so that sophisticated financial market, improved financial instruments as well as efficient and effective financial process can be developed. Presently there is proliferation of various banking and non banking financial institutions in the country offering wide range of services including much new type of financial services like venture capital, leasing, merchant banking, mutual fund etc.

Among such new financial services leasing is one of the innovative financial service, which carry extremely different philosophical idea about the use of capital asset in productive activities. Leasing concept advocate that the important thing is the service we get from using asset, not the ownership on it. Therefore, it is wise to take service of any asset in rental basis without purchasing it.

Leasing industry has made invaluable contribution towards the small and medium business in Nepal. Because of key role the small and medium business have played in accelerating economic development therefore credit must goes to leasing companies.

Its strength is not only limited to uplift the industrial sector by Vehicles, Tools and Equipment Lease financing but also to uplift the standard of living of people by household appliances and other assets lease financing

As the finance companies' performance has been hindered by the economic situation of the country. And if the political and economic situation of the country improves then the leasing industry can be viewed as the cupid in the horizon.

4.10 Problems of Leasing Business in Nepal

-) Leasing being the new concept for the Nepalese financial sector, there are problems in almost all the dimensions of leasing business. The problems faced by Nepalese leasing business are stated as follows: The first and the foremost problem that the leasing business in Nepal facing is the lack of the proper and unique act that is solely made for the leasing purpose. The finance companies are required to perform the leasing business according to the provisions made under Finance Company Act 1986, Contract Act 2000, NRB directives, Income Tax Act 2001 and foreign exchange (regulation) Act 1955 second amendment on 2002 of Nepal. Every finance company feels the need of the leasing act so that there exist the smooth and parallel way of performing leasing business among the finance companies.
-) The lack of capital is one of the prominent problems for the finance companies. Due to this the finance companies are not able to invest in the equipments that cost very high. So they are limited only up to financing business like hire purchase of two-wheeler and small four-wheelers, etc. The finance companies with limited low capital need to expand their capital in order to enter the leasing business.

-) The most common problem faced by all the finance companies is the recovery problem. The recovery problem means the delay and default in the payment of the monthly rental. This problem has risen due to the low economic conditions of the country. But for this problem, the finance companies have little different view. They say that it is not only the economic condition of the country but it has more to do with the capacity of the lessee to perform his/her business successfully regardless of hindrances they face. To the some extent finance companies also held responsible for this problem, as the finance companies may have failed to find the credibility of the perspective client from the NRB's credit information bureau or some other financial institutions with whom the perspective has performed any sort of business.
-) The other problem faced is the difficulty in identification of the vehicles in case of the used vehicles. It is very difficult for the finance companies to identify the value of the asset and the condition of the asset. In such case of leasing of used vehicles, the company charges higher percentage as a down payment. This makes the lessee difficult to provide such amount, which may lead to disagreement between the two parties and may end up without signing a lease contract.
-) The finance company when receives the rental, it is treated as the income earned and the finance companies have to pay tax on the capital recovered also as the rental includes the portion of capital recovered and interest. This can be termed as tax loss incurred on capital recovery. The finance companies usually face heavy tax loss during the initial years and can only gain on tax in the concluding year. The tax loss may be recovered by the tax gain on depreciation of the leased asset, however, if we consider the time value of money, then the finance companies will be in loss. The prevailing rate of depreciation discourages the leasing business in Nepal.

-) The study has found that there has been difference in the knowledge of leasing amongst the leasing/finance companies also. Every sample organization seems to possess different knowledge of leasing and different techniques in calculating lease rental. This procedure has an adverse effect on the clients, as they were unable to decide which finance company to choose for the leasing. This may reduce the perspective client, as they may prefer borrowing instead of leasing, which will reduce the benefits that may be availed from the leasing.
-) Usually for any business a business-person seeks for the bigger market. Nepal being a smaller market and financial institutions are hesitating to enter the industry. But the Nepalese leasing market is not small as they has opined. This concept has prevailed in their mind since their establishment. And because not too many surveys and researches have been made in this area, finance companies are unknown of the existing prospects of investment in small-scale industries. The lack of detailed survey is what the finance companies are seeking for and they cannot do it on their own as of lack of capital to be invested in such research.

Being the new concept for the Nepalese financial sector, there are problems in almost all the dimensions of leasing business. Companies under study have ranked their problem as high credit risk in the business, market problem, capital problem, management problem and legal problem in most dominated to least dominated form.

4.11 Challenges of leasing Business in Nepal

Leasing business in Nepal is in its developing stage and with that there exists many challenges. The foremost challenge is the trust or faith between the clients and the financial institutions. The financial institutions usually do not have the trust of faith on its perspective client. This problem has probably arisen due to the current economic situation of this country and this problem may continue if the economic situation of this country does not improve. Low

economic conditions can lead to lower profits in the business and the lessor may hesitate to invest in the people with whom the lessors have never dealt. The probable client of the lease finance can be a juvenile but may have lots of enthusiasm to do the business, upon which the lessor does not have full trust. The lessors have trust either on the older clients or to some big business persons whom they have known to perform successful business. These lacks of trust between the clients and the finance companies have been one of the important challenges of the leasing business.

Finance companies are required to keep their investment in the safe side. So it has to keep the collateral to safeguard their investment. And the clients usually have complains that the finance companies asks too much collateral. This perception should be changed as the collateral is only for the security purpose, which the client must keep with the finance company to maintain the good professional relationship. If the client opposes for the collateral, then the finance company shall have doubt on the perspective client's performance. And the lessor/finance company may hesitate to give loan or invest on lease finance.

There has been the concept among the lessee or clients that if they have provided the collateral more than the loan amount, then the borrower have to obey the finance companies. And if the finance company extends the loan amount without the further collateral then the finance companies have to obey its clients. This prevailing thought has led to low professional relationship between the two parties. These thoughts should be removed from the mind of general people or the perspective client in order to improve the relationship between clients and the finance companies.

There are also other practices going on unfavorable to the finance companies that the clients being bankrupt are easily allowed to start other business, getting loan from another financial institutions. This is because there is no system available to keep a track record of the borrower and these systems should be changed to keep the lease financing business safe. These types of practices can

lead to mal practice by the user of the fund. Borrowers may not perform well in their business as, if their business goes wrong, then they can liquidate their business and will not be stopped from doing other business by taking loans from another financial institutions.

4.12 Major Findings of the Study

-) There does not exist any specific act related to the leasing business.
-) The “Finance Company Act 1986” is only act which has provided legal rights to finance companies to perform the leasing business.
-) Section 3 of the act has laid down that finance companies can make available leasing finance to any individual, firm, company or institution for purchase of vehicles, machinery and tools equipment and durable household goods or similar movable property.
-) It is further found that except finance companies, no other financial institutions like commercial banks, insurance companies are legally allowed to do leasing business.
-) Though the finance companies act open the door for leasing business in 1986 leasing business found actually being performed in 1995.
-) Beside Finance Company Act 1986, other acts and rules like Contract Act 2001, Nepal Rastra Bank Act 2001, Income Tax Act 2001 and directives issued

Nepal Rastra Bank to the finance companies are found as other major applicable laws.

-) The lease finance should not exceed 20 percent of the total credit.
-) There are only four finance companies doing leasing business, of which three are operating from inside the Kathmandu valley and only one from outside the Kathmandu valley from Hetauda.

-) Despite of two consecutive years of negative growth in lease finance, Nepalese lease finance market has been able to sustain the positive growth rate.
-) It has been found that ILFC and UFCO are only two finance companies having greater share in total lease finance and to be known as the *pioneers* of the lease finance industry.
-) Share of lease finance in total credit is very nominal in the year 2061/62 B.S and is about 3.02 percent but it decline to 0.78 percent in the year 2063/64 and for the year 2064/65 B.S it slightly increase to 1.16 percent.
-) Regarding the renewal of lease, it found that ILFC and NSLMB provide the facility of renewing lease but UFCO does not renew the lease for secondary period. In case when the lease is renewed, lease rental, structure of collection, stipulated loss values are changed. Other terms and conditions remain same.
-) Insurance of the leased asset is compulsory and the lessee bares the expenses indulged.
-) It is further found that all the companies require certain deposit or security from the lessee on lease execution date in order to secure the performance of all obligation of the lessee.
-) It was found that all three finance companies have different way of calculating the lease rental and the schedule of payment.
-) Though the fundamental of leasing is to take rental in advance, it was found that NSLMB takes rental at the end of the month.
-) The deposit required by NSLMB is termed as the Down Payment, the deposit required by the UFCO is termed as Major Rental and the deposit required by the ILFC is termed as Key Money.
-) There has not been proportionate increment in leasing business in accordance to other investments like loan and advances.
-) ILFCO invest more amount of their fund in lease finance whereas Union finance, NSLMB and WMBFCO comes to second, third and fourth.

-) There is a huge fluctuation in lease finance of WMBFCO and to certain extent Union finance also suffers regarding this matter in compare to ILFCO and NSLMB.
-) It is found that ILFCO and NSLMB emphasis more of their lease finance on Vehicles where as Union Finance emphasis on Tools and Equipment.
-) It is found that all the finance co. invest nearly same ratio of their fund in lease finance from their loan and advance as the calculated value of F test on the percent of lease finance from loan and advance is less than tabulated value, there is homogeneity in mean value .
-) Last five years data reflects that there is no homogeneity in the contribution of lease finance of three finance co. from total lease but when we segregate the lease finance into Vehicles & Tools and Equipment Lease finance, we can find that there is only homogeneity in the contribution of Tools and Equipment lease Finance.
-) ILFCO, Union Finance and NSLMB being the pioneer companies for leasing business has not been able to invest significant amount of their fund in lease finance from their deposit. As $r < 6PEr$ of all three finance co we can further conclude that the relationship between total deposit and lease finance is not significant. But the correlation (r) of ILFCO is only positive among three finance co so, to certain extent its investment from deposit can be considered as satisfactory.
-) None of the finance companies are assured that existing infrastructures for doing leasing business prevailing in the country are sufficient. Rather 88 percent companies have opined that existing infrastructures are not sufficient. 12 percent of the companies are found unknown to the fact.
-) Regarding the need of operating leasing in the country, 66 percent of the finance companies have opined that there is the need for developing operating leasing. Although, none of the finance companies have apposed it, 32 percent are unknown to the need of operating leasing.

-) Regarding the appropriateness of income tax for the development of leasing business, 75 percent of the finance companies think that current income tax is not favorable for the development of leasing business. None of the finance companies have agreed that income tax is favorable. One-fourth part of the finance companies are found unknown about the appropriateness of the income tax law for leasing business.
-) It is found that; legal problem in leasing business remained as the most dominant problem due to which finance companies are not entering into leasing industry. High credit risk is found to be the second dominant problem. Likewise lack of market, capital problem and management problem are found third, fourth and fifth dominant problem respectively.
- A
-) In order to achieve the bright prospect of leasing business in Nepal, it is found that these activities must be done i.e. Legal provision should be enacted, effort for publicity should be made, tax and other incentive should be provided, skilled manpower should be developed and present practice should be made effective.
-) It is found that, there is no presence of lease broker in Nepalese leasing industry that provides advisory and technical services in the selection and structuring of lease.

CHAPTER-V

SUMMARY, CONCLUSION AND RECOMMENDATIONS

5.1 Summary

The main objective of the study was to find the practices followed by the leasing companies regarding lease and its problems and prospects of leasing business in Nepal. To attain the objective of the study, various analytical and descriptive techniques have been used.

These studies comprises of identification of the history of financial institutions and the leasing business performed by the finance companies. The history of Nepalese financial institutions has been going on since the ancient time, which started with the act of giving loan to the needy people by the people who have excess money upon deposit of some collateral. This system of transaction prevailed until the government started organized business, which led to today's modern age of financial transaction through banks and finance companies. Today there are 17 commercial banks and 59 non-bank financial institutions performing financial transaction in Nepal.

Leasing business is a new concept for Nepalese financial market. It is only ten years old and there are only 2 finance companies performing leasing business in Nepal. To name them, they are: Union Finance Company (UFCO), International Leasing and Finance Company (ILFC), Nepal Sri Lanka Merchant Bank (NSLMB) and World Merchant Bank and Finance Company (WMBFC). Though the study has found that there exist both financial and operating lease, most of the share in uses of funds in leasing has been occupied by the financial lease. The highest contribution in 2005 A.D. the total lease is contributed by IFC (around 52 percent). The UFCO, NSLMB and WMBFC have the 37 percent, 7 percent and 2 percent respectively. The study has revealed that though the situation has not been favorable, the lease finance has

the growing trend. The uses of funds in lease finance for the year 2005 A.D. was Rs.363.6 million.

It has been almost ten years since the first leasing business started with the establishment of Union Finance Company in the year 1995 A.D. and till today there does not exist a specific act solely made for leasing business. The Finance Companies Act 1986 is the act, which has provided the legal right to finance companies for carrying leasing business in Nepal. Other Acts like, Contract Act 2000, Income Tax Act 2001, NRB Directives issued in the interest of finance companies and other notices from NRB, governs leasing business in Nepal.

The sample companies have relatively similar clauses in the lease contract. The asset to be leased is determined by the lessee and the lessor usually appoints the supplier in order to protect the lessor's interest from being deluded by the bad intension of the lessee. Each finance company requires its rental to be paid monthly and in advance except NSLMB. The lessee is required to pay the interest on any overdue amount to the lessor or the finance company. The lessor also doesn't take any responsibility regarding the guarantees provided by the supplier/manufacturer; however, the lessor may help the lessee to get his right upon submission of the written request. All the finance companies needs that the leased assets should be operated only in the area proposed and only for the task proposed. The repair and maintenance of the leased asset is to be done entirely by lessee at its own expense and any part attached in the asset with the consent of the lessor, the attached part also becomes the property of the lessor. And the insurance of the leased asset is also bared by the lessee and may be paid through the lessor's account. Upon non-performance of the clauses of the lease contract, the contract terminated and termed as default. The lessee is liable to pay all the amounts due to the lessor upon termination by default, as if any amount is due had the contract continued.

The lease rental is the integral part of the lease finance. And all the sample organization uses different ways of calculating the lease rental by using computer software of their own. The UFCO though doesn't use any additional software to calculate the lease rental. The lease rental is obtained by entering the data in the fields of the software to get the results. The schedule of payment also varies from one to another as all the finance companies uses different ways of treating the bulk amount taken at the beginning of the contract. NSLMB regards it as part of loan and deducts it from total lease finance to calculate the lease. UFCO takes the amount as the major rental, which includes the principal and the interest portion and only the principal portion is deducted to get the equal monthly rental. ILFC takes such amount as a deposit, so, it calculates rental by taking all of the cost of the assets and upon successful completion of the contract it is refunded to the lessee.

There are not any areas in the world free of problems and so do the leasing business in Nepal. The first and the prime problem is that the leasing business in Nepal till today is being performed without any specific leasing act. Due to this the finance companies have different views and ways of treating lease finance, making the clients difficult to compare and to choose between the existing finance companies. Desperate need of the leasing act has been felt to bring about the parallel way of leasing business amongst the country and to expand the business. The other problem is the lack of capital. Huge amount is needed to expand the business or to target the large industries. Though the finance companies have entered into the leasing industry, they face different problems. The first problem is with the credibility of the lessee as finance companies struggles to find the credit history of the perspective client. They also face the problem of recovery of the rentals or with the untimely payment of the lease rentals. It is also very difficult to identify the state of the used assets to give it some standard to categorize it on the basis of good, indicative, substandard, doubtful and bad. The finance companies are struggling to enhance the features of the lease to benefit both the parties. They are seeking

for the market to invest and are destitute to have a thorough research in the lease market.

The finance companies face great challenges to build faith among them. Finance companies usually do not have faith on new clients regardless of their capability, which should be changed to bring about the trust among themselves to bring livelihood in the leasing business. The other challenge is to convince the customer that the collateral is for the security purpose only, not to give trouble to the lessee. The finance company may doubt on the client if the client opposes for the collateral and should find about the credibility of the perspective before turning it to the client. There is another challenge for the finance companies to remove the misconception that, if lessee have provided the collateral more than the loan amount, then the borrower have to obey the finance companies And if the finance company extends the loan amount without the further collateral then the finance companies have to obey its clients. The bad client or the lessee, who has attempted a fraud, should be stopped from doing another business but here such person can easily get loan from another financial institutions and start another business. The government or the concerned authority should eliminate these things in order to protect the rights of the financial institutions.

5.2 Conclusion

The research has gone through thorough investigation and analysis of the findings. And upon studying the whole findings and analysis, this part of the research is an attempt to conclude the thesis by some final drawing some conclusions.

Since the leasing business is only about ten years old and with only four finance companies into leasing industry, it can be said that the lease financing is its infantry stage. The appropriateness and its effectiveness in contributing to the country's economy have yet to be assessed. Lot more finance companies

are needed to enter the market. Leasing seems to be overlooked or ignored by the government or the concerned authorities. Even the finance companies that have entered the lease industry are not running it successfully or rather can be said that finance companies have not taken lease finance as high priority. Only ILFC and UFCO have significant contribution in the lease market. The other two institutions need to improve their market share. However the lease finance has managed to multiply largely during its journey till today and could be said that the finance companies are doing well.

Lease business has not been able to flourish as it would have been if there had been a separate act for it. All the finance companies have different ways of treating the lease finance and this indicates the need of the separate act. Lease finance has been treated just as other loans provided. This has created many legal uncertainties and thus the leasing business has not been able to foster. Need of separate and unique act for the leasing has been felt by all the finance companies and that is the bottom line.

Upon studying the clauses in the lease contract, it was found that the contract has kept the lessor at the safe side and free of many responsibilities. This is definitely good for the finance companies but the lessees may not benefit from those clauses. There are few rights to the lessor and wholesome burdens of responsibilities on the part of lessee. Though the finance companies are in safe side with regard to clauses of the contract, there have been cases of loss to the lessor also and this shows the weakness of the finance companies to get the credit information of the client.

5.3 Recommendations

The detailed study has revealed many facts and findings of the leasing business in Nepal. On the basis of these findings, the researcher has made the following recommendation and suggestion to overcome the present weakness and

inefficiencies as well as utilize opportunities and to improve and develop the leasing business in this country.

-) Concerned authorities should start to initiate to bring the leasing act so that the finance companies will be able to bring the parallel way of performing leasing business. The separate leasing act will help to introduce an independent leasing company that will be doing leasing businesses only.
-) The finance companies have opined that the prevailing depreciation rate has discouraged the leasing business many times. So it is recommended to increase the depreciation rate so that the enthusiasm created in the lessor could bring in the revolution the leasing business.
-) The finance companies' contract bears the clauses that give more right and less responsibility to the lessor and less right and more responsibilities to the lessee. This situation of unequal right and responsibility bearing is not optimal for the development of the lease. It is recommended to finance companies to balance the rights and responsibilities.
-) The finance companies in Nepal are unable to create a faith with the perspective client. They only believe on the big business houses or the older clients. The finance companies should get enough credit information of the perspective or if the client is juvenile then thorough investigation can be made on the business proposal the perspective has presented to get its asset leased.
-) Tax is the greatest strategic consideration for business organization as well as for the government. Government use tax as an effective measure for channeling available resources in the country. Literature has shown that fundamental reason behind development leasing activities is the tax concession provided to the leasing companies and user of the leasing service in those countries where economic boost has been achieved after adoption of leasing. In Nepal, current Income tax Act has not provided

tax concession to the companies carrying leasing and user of the lease service. This research recommends to provide tax concession to both the parties because such tax concession would not results into loss in the revenue to the government rather is generate speedily in economic activities from which tax loss is compensated and economy is uplifted.

-) Foreign exchange (Regulation) act has not made any provision relating to the transaction made under international or cross boarder leasing. The provision, made in general, create difficulties for efficient and effective implementation to leasing deal. It is, therefore, recommended that special provision for the transaction of international leasing are to be included in foreign exchange (Regulation) Act till the enactment of special leasing act.
-) The general public of this country do not have the clear concept of lease financing and its benefits. The finance companies are required to market their product in the local market so that the smallest business can also benefit by getting the desired asset leased instead of borrow. The adequate marketing of the lease is a must to increase the awareness of leasing business among general public. This would help to increase the leasing business in Nepal.
-) ILFCO and NSLMB invest less amount of fund in Tools and Equipment lease finance. But country like Nepal seeks more lease finance on Tools and Equipment as small and medium scale industries can benefit the advantage of lease which will ultimately uplift the development of industry in a country.
-) It is found that NSLMB and Union finance invest less amount of their fund from the deposit. Being the pioneer of leasing business, instead of investing huge fund in lease to develop leasing business, they overlooked leasing business. So, they are recommended to invest more funds in lease finance so that other finance co could able to get inspiration from them.

-) It has been found that even NRB has not made clear vision regarding leasing business and is not actively creating conducive environment for the development of leasing activities. This could be one of the major hindrances for the development of leasing activities in the country. NRB Act has empowered NRB to lead the banking and financial system of the country. Thus it can play significant role in the development of leasing business. Therefore NRB is recommended to assess the macro economic impact of the leasing activities and make policy accordingly.
-) Eighty four percent of the total finance companies have opined that 25 crore capital required for carrying leasing business is to be reduced. Finance companies in Nepal still have not gained full confidence of public. They may not be able to raise such a huge capital. In such situation only few companies can enter into industry and therefore leasing will not be practiced widely. Hence, NRB is recommended to re-think the applicability of this capital requirement provision.
-) Eighty eight percent of the finance companies have thought that existing infrastructures for carrying leasing business are not sufficient. This has clearly reflected the need to be focused on development of necessary infrastructure. Companies will not be ready to carry leasing business until they think those infrastructures are sufficient. Therefore, it is recommended that any development strategy should give priority to the development of necessary infrastructure for carrying leasing business first.

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Annex-1
FINANCIAL INSTITUTION IN NEPAL

	Financial Institution	Place	Estd.	Amount in Million
Commercial Banks				
1	Nepal Bank Limited	Kathmandu	1994.07.30	3804
2	Rastriya Banijya Bank	Kathmandu	2022.10.10	11723
3	Nabil Bank Limited	Kathmandu	2041.13.29	4917
4	Nepal Investment Bank Ltd.	Kathmandu	2042.11.26	2953
5	Standard Chartered Bank Nepal Ltd.	Kathmandu	2043.10.16	3746
6	Himalayan Bank Ltd.	Kathmandu	2049.10.05	5363
7	Nepal SBI Bank Ltd.	Kathmandu	2050.03.23	4319
8	Nepal Bangladesh Bank Ltd.	Kathmandu	2050.02.23	7025
9	Everst Bank Ltd.	Kathmandu	2051.07.01	4550
10	Bank of Kathmandu Ltd.	Kathmandu	2051.11.28	4636
11	Nepal Credit and Commerce Bank Ltd	Siddharthanagar	2053.06.28	5950
12	Nepal Industrial and Commercial Bank Ltd.	Biratnagar	2055.04.05	5000
13	Lumbini Bank Ltd.	Narayangadh	2055.04.01	5000
14	Machapuchre Bank Ltd.	Pokhara	2057.06.17	5500
15	Kumari Bank Ltd.	Kathmandu	2057.12.21	5000
16	Laxmi Bank Ltd.	Birjung	2058.12.21	6097
17	Siddhartha Bank Ltd.	Kathmandu	2059.09.09	3500
Developmental Bank				
1	Agricultural Developmental bank	Kathmandu	2024	15469
2	Nepal Industrial Development Corporation	Kathmandu	2016	4158
3	Nepal Development Bank Ltd.	Kathmandu	2055	1440
4	Entrepreneur Development Bank Ltd.	Chitwan	2055	82
5	Nirdhan Uttham Bank Ltd.	Siddharthanagar	2055	990
6	Mallika Development BankLtd.	Tikapur, Kailali	2055	140
7	Rural Micro Finance Developmental Bank Ltd.	Kathmandu	2056	800
8	Siddhartha Development Bank Ltd.	Butwal	2055	104
9	Development Credit Bank Ltd.	Kathmandu	2057	1600
10	United Development Bank Ltd.	Bara	2058	108
11	Nepal Cottage and Small Industry Development Bank Ltd.	Kathmandu	2058	1120
12	D-Prox Development Bank	Chitwan	2058	1600
13	Narayani Industrial Developmental Bank	Chitwan	2058	140
14	Chhimek Development Bank Ltd.	Hateuda	2058	100

15	Swalamban Development Bank]	Janakpur	2051	126
16	Small Farmer Development Bank Ltd.	Kathmandu	2058	1051
17	Western Development Bank Ltd.	Rupandehi	2051	200
18	Sahayogi Development Bank Ltd.	Janakpur	2058	140
19	Pashupati Development Bank Ltd.	Banepa	2051	2000
20	Karnali Development Bank Ltd.	Nepalgunj	2060	102
21	Triveni Development Bank Ltd.	Chitwan	2060	175
22	Annapurna Development Bank Ltd.	Banepa	2060	102
23	Brikuti Development Bank Ltd.	Rupendehi	2061	150
24	Subheksh Development Bank Ltd.	Chitwan	2061	140
25	Bageshwori Development Bank Ltd.	Nepalgunj	2061	140
26	Sanima Development and Finance Institution	Kathmandu	2061	1632
27	Gauri Shankar Development and Finance Institution	Navalparasi	2061	120
28	Gorkah Development Bank	Kathmandu	2061	1633
28	Vibor Development Bank	Kathmandu	2063	
29	Birat Laxmi Development Bank	Biratnagar	2063	
30	Kankai Bikas Bank	Damak	2063	100
Rural Development Banks				
1	Estern Rural Development Banks Ltd.	Biratnagar	2049	600
2	Far Western Rural Development Banks Ltd.	Dhangadi	2049	600
3	Western Rural Development Banks Ltd	Butwal	2051	600
4	Mid-western Rural Development Banks Ltd.	Nepalgunj	2051	600
5	Middle Zone Rural Development Banks Ltd.	Janakpur	2053	600
Finance Company				
1	Nepal Housing Development Finance Company	Kathmandu	2049	482
2	N.I.D.C. Capital Market Limited	Kathmandu	2049	580
3	Nepal Finance and Saving Company Limited	Kathmandu	2049	200
4	National Finance Company Limited	Kathmandu	2050	360
5	Annapurna Finance Company Limited	Pokhara	2050	300
6	Nepal Share Market and Finance Limited	Kathmandu	2050	1200
7	Peoples Finance Limited	Kathmandu	2051	313
8	Mercantile Finance Company Limited	Birjung	2051	180
9	Kathmandu Finance Company Limited	Kathmandu	2051	300
10	Himalayan Finance & Saving Company Limited	Kathmandu	2051	330
11	Union Finance Company Limited	Kathmandu	2051	600
12	Narayani Fianance Company Limited	Bharatpur	2051	355
13	Gorkah Finance Limited	Kathmandu	2051	250
14	Paschimanchal Finance Company Limited	Butwal	2051	400

15	Nepal Housing and Merchant Finance Limited	Kathmandu	2051	495
16	Universal Finance Limited	Kathmandu	2052	315
17	Samjhana Finance Company Limited	Banepa	2052	212
18	Goodwill Finance Limited	Kathmandu	2052	250
19	Siddhartha Finance Limited	Siddharthanagar	2052	40
20	Shree Investment & Finance Company Limited	Kathmandu	2052	400
21	Lumbini Finance & Leasing Company Limited	Kathmandu	2052	510
22	Investa Finance Limited	Birgunj	2052	240
23	Yeti Finance Limited	Hetauda	2052	200
24	Standard Finance Limited	Kathmandu	2052	600
25	S. Finance Company Limited	Kathmandu	2052	900
26	International Leasing & Finance Company Ltd.	Kathmandu	2052	1200
27	Mahalaxmi Finance Ltd.	Birgunj	2052	500
28	Lalitpur Finance Company Ltd.	Lalitpur	2052	338
29	Bhajuratha Finance & Saving Company Ltd.	Kathmandu	2052	210
30	United Finance & Saving Company Ltd.	Kathmandu	2052	600
31	United Finance Company Ltd.	Kathmandu	2052	191
32	General Finance Ltd.	Kathmandu	2052	1000
33	Nepal Sri Lanka Merchant Bank Ltd.	Kathmandu	2052	147
34	Merchant Finance Company Ltd.	Kathmandu	2052	400
35	Elpic Everest Finance Ltd.	Kathmandu	2053	1000
36	Nepal Merchant Banking & Finance Ltd.	Bhaktapur	2053	200
37	Navadurga Finance Company Ltd.	Janakpur	2053	200
38	Janki Finance Company Ltd.	Pokhara	2053	200
39	Central Finance Company Ltd.	Kupondle	2054	200
40	Premium Finance Company Ltd.	Lalitpur	2054	200
41	Arun Finance and Saving Company Ltd.	Dharan	2054	60
42	Multipurpose Saving & Investment Company Ltd.	Rajbiraj	2055	30
43	Butuwal Finance Ltd.	Butwal	2055	500
44	Srijana Finance Ltd.1	Lahan	2056	60
45	Nepal Bangladesh Finance & Leasing Co. Ltd.	Biratnagar	2056	500
46	Om Finance Ltd.	Pokhara	2057	200
47	Cosmic Merchant Banking & Finance Company	Kathmandu	2057	600
48	World Merchant banking & Finance Ltd.	Hetauda	2058	600
49	Capital Merchant Banking & Finance Ltd.	Kathmandu	2058	305
50	Crystal Finance Ltd.	Kathmandu	2058	263
51	Royal Merchant Banking & Finance Ltd.	Kathmandu	2058	300
52	Guheshwori Merchant Banking & Finance Ltd.	Lalitpur	2059	182

53	Patan Finance Company Ltd.	Lalitpur	2059	300
54	Cryst Merchant Banking & Finance Ltd.	Kathmandu	2059	500
55	Fewa Finance Company Ltd.	Pokhara	2060	200
56	Everest Finance Ltd.	Siddharthanagar	2060	120
57	Birjung Finance Ltd.	Birgunj	2060	600
58	Prudential Merchant Banking & Finance Ltd.	Kathmandu	2061	255
59	Investment and Credit Finance Company Ltd.	Kathmandu	2061	255
Co-Operative Institutions				
1	Navjivan Co-Operative Institution Ltd.	Dhangadi	2058	135
2	Sagun Co-Operative Institution Ltd.	Kathmandu	2051	111
3	Nepal Co-Operative & Finance Institution Ltd.	Kathmandu	2051	147
4	Kakalu Transport & Co-Operative Institution Ltd.	Biratnagar	2051	32
5	The Sahara Loan Saving and Investment Co-Operative Society	Malangawa	2052	208
6	Bindwasini Saving and Loan Co-Operative Institution Ltd.	Kavre	2052	-
7	Mahila Co-Operative Society Ltd.	Kathmandu	2052	106
8	Nepal Multipurpose Co-Operative Society Ltd.	Jhapa	2052	80
9	Raj-Shree Savings & Investment Co-Operative Society	Malangawa	2052	144
10	Co-Operative Finance & Development Society	Nepalgunj	2053	64
11	Shree Manakamana Co-Operative Society Ltd.	Kavre	2053	81
12	Veri Co-Operative Society Ltd	Nepalgunj	2053	48
13	Viku Savings and Loan Co-Operative Society Ltd.	Navalparasi	2054	28
14	Amarawati Multipurpose Co-Operative Society Ltd.	Kathmandu	2054	75
15	Farmer Multipurpose Co-Operative Society Ltd.	Kailali	2054	30
16	United Savings & Loan Co-Operative Society Ltd.	Kathmandu	2054	107
17	Himalayan Co-Operative Society Ltd	Kathmandu	2055	336
18	Star Multipurpose Savings & Loan Co-Operative Society Ltd.	Biratnagar	2055	
19	Yeti Savins & Loan Co-Operative Society Ltd.	Kathmandu	2055	21
20	Upkar Savings & Loan Co-Operative Society Ltd.	Syangja		58
Non Government Institution (Micro Finance)				
1	Nepal Village Development Society Center	Biratnagar	2056	11
2	Nepal Village Development Institution	Kathmandu	2057	3340

3	Nepal Sikara Village Development Programme	Chitwan	2057	
4	Four Star Youth Club	Baglung	2057	424
5	Mahuli Samudiak Development Center	Saptari	2057	
6	Samuhik Youth Club	Bardiya	2057	566
7	Samudaik Mahila Development Center	Saptari	2057	1500
8	Gramin Samudayako Lagi Yojana Prtyabhuti Samooch Nepal	Dhankuta	2057	
9	Gramin Jagran Mantra	Baglung	2057	
10	Sarvoday Village Development Society	Saptari	2057	255
11	Human Development Society	Rasuwa	2057	
12	National Educational And Social Development Institute	Kushma	2057	111
13	Dhaulagiri Social Source Development Center	Baglung	2057	0.3
14	Nepal Vatavaran Tatha Pradushan Unmulan Youesco club	Kathmandu	2057	
15	Vikash ka lagi Sthaniya Swayam Sewakharuko Prayas	Dhankuta	2058	127
16	Nepal Women's' Entrepreneur Society	Lalitpur	2058	30
17	Mahila Adhikar Thatha Vikas Kendra	Kathmandu	2058	1146
18	Manusi	Kathmandu	2058	
19	Jeevan Viaks Samaaj	Morang	2059	
20	Nari Utthan Tatha Balbalika Sangrakshan Sang	Saptari	2059	
21	Manila Adarsh Sewa Kendra	Kathmandu	2059	
22	Patan Business and Professional Women	Lalitpur	2059	126
23	Nari Uththan Kendra	Chitwan	2059	
24	Mahila Swawlamban Samaaj	Chitwan	2059	
25	Nepal mahila Utthan Kendra	Lalitpur	2059	575
26	Bhagan Yuva Club	Kathmandu	2059	
27	Srijanatmak Mahila Vatavarna Sanstha	Kathmandu	2059	35
28	Srijana Samudaik Vikas Kendra	Siraha	2059	164
29	Srijana Vikas Kendra	Pokhara	2059	
30	Singana Yuva Club	Baglung	2059	2090
31	Cottage and Small Development Society	Kathmandu	2059	3654
32	Amma Samaaj Sangh	Parvat	2059	
33	Adarsh Yuvak Club	Bhaktapur	2059	
34	Society Welfare Action Nepal	Dang	2059	
35	Social Upgrade in Progress of Education Reason	Dang	2059	
36	Nepal Mahila Samudaik Sewa Kendra	Dang	2059	

37	Gramin Mahila Utsukta Vikas Kendra	Sunsari	2059	
38	Gramin Mahila Vikas Sanstha	Chitwan	2059	1503
39	Amma Samaaj Sangh	Dang	2060	
40	Gramin Mahila Utthan Kendra	Dang	2060	
41	Khurkot Yuva Club	Parvat	2060	
42	Tharu Tatha Raji Mahila Samaj	Kailali	2060	
43	Nari Abhyudya Kendra	Narayangadh	2060	164
44	Mahila Upkar Manch	Bankey	2060	
45	Chhimek Samaaj sewa Sansthan	Kathmandu	2060	
46	Swalamban Development Center	Kathmandu	2061	5826
47	Vikas Aayojana Sewa Kendra	Kathmandu	2061	

Sources: Banking Khabar Patra

Annex-2

QUESTIONNAIRE

Name: Designation:

Office/Organization:.....

Occupation:

This questionnaire is concerned with the study on "**Problem and Prospects of Leasing Business in Nepal**". It would be very much appreciated if you could spare some of your valuable time for filling this questionnaire.

1. In your opinion, is the infrastructure for leasing business is sufficient?
a. Yes () b. No. () c. Don't Know ()
2. Do you think that the present time is appropriate to start leasing business?
a. Yes () b. No. () c. Don't Know ()
3. In your opinion, the finance companies have realized the need of operating leasing?
a. Yes () b. No () c. Don't Know ()
4. If no, please specify
.....
.....
5. Do you think that the tax concession provided by the income tax plays most important role for the leasing business?
a. Favorbale() b. Unfavorable () c. Don't Know ()
6. In Your Opinion, is the NRB has clear vision about Leasing Business?
(a) Yes () (b) No () c. Don't Know ()
7. Do you think, the provision of NRB regarding leasing business is appropriate or not?
a. Appropriate () b. Need to reduce() c. Need to increase()

8. What is the major problems of the finance company faces in leasing business?
- a. Absent of Lease Act ()
 - b. High credit Risk ()
 - c. Lack of Market ()
 - d. Lack of Capital ()
 - e. Management Problem ()
9. What are the important factors needed for successful leasing business in Future?
- a. Credit assessment expertise ()
 - b. Speed in utilization of fund ()
 - c. Cheap source of fund ()
 - d. Searching new market and flexibility in lease operation ()
10. What is the future prospect of leasing business in Nepal? ()
- a. Excellent ()
 - b. Good ()
 - c. Satisfactory()
 - d. Fair ()
 - e. Good ()
11. What should be done to ensure bright prospect of leasing business in Nepal?
- a. Clear Legal Framework regarding the leasing business()
 - b. Effort for the publicity ()
 - c. Provision of tax ()
 - d. Incentive ()
 - e. Development of skilled manpower ()

"Thank You for Your Kind Co-operation"

Annex-3

GROWTH OF LEASING INVESTMENT

Year (n)	Total Loans & Advances on Lease Finance(Y)	X=(n-2003)	X ²	XY	Trend Value Y _C =a+bX
1998	26.3	-5	25	-131.5	141.21
1999	52.5	-4	16	-210	153.06
2000	185	-3	9	-555	164.91
2001	310.3	-2	4	-620.6	176.76
2002	260.1	-1	1	-260.1	188.61
2003	235.3	0	0	0	200.46
2004	277.8	1	1	277.8	212.31
2005	363.6	2	4	727.2	224.16
2006	128.8	3	9	386.4	236.01
2007	138.2	4	16	552.8	247.86
2008	227.2	5	25	1136	259.71
N=11	Y =2205.1		X ² =110	XY X1303	

$$a X \frac{Y}{N}$$

$$b X \frac{X^2}{XY}$$

Future Forecast of Lease Finance

Year	X=(n-2005)	Y=a-bX
2009	4	153.06
2010	5	141.21
2011	6	129.36
2012	7	117.51