

XIX. Borrowings

21. *There being no constitutional requirements relating to borrowings and there still being a need for making adequate provisions in the municipal laws relating to the same, the question is as to what provisions may be made for extensive coverage of this subject.*

- (1) State Governments, while considering the relevant issues, may keep in view the facts that the legislative schemes in the various municipal laws provide for powers of the municipal governments to borrow money or raise loans, issue debentures, create sinking funds and invest the amounts in the sinking funds. These laws also specify the agencies from which loans may be taken and whether State Government guarantees are mandatory or not. *The Acts, as of now, do not provide for the role of any credit rating agencies as approved by the Central Government or the State Government.*
- (2) As regards the borrowing powers, the Calcutta, Bombay, Gujarat, Madhya Pradesh and Tamil Nadu Acts have very specific provisions. Of these, the Bombay, Calcutta, Madhya Pradesh and Tamil Nadu Acts also specify the limits to the power of raising loans.
- (3) The Tamil Nadu Urban Local Bodies Act, 1998, which is the latest in the series of new Acts, under section 66, provides that the Municipality may borrow money by way of debentures, by raising loans from any scheduled or nationalized bank, or from any other financial institution or agency, as may be approved by the State Government in this behalf, on the security of all or any of the taxes, duties, fees and dues authorized by, or under, this Act, *for the purposes as may be determined by the State Government.* It also provides for raising loan from the public by issue of bonds for incurring specific items of capital expenditure.

It further provides that the amount of loan, the rate of interest and the terms including the date of floatation, the time and method of repayments shall be subject to the approval of the State Government.

- (4) Section 110 of the Gujarat Act and section 109C of the Bombay Act also provide for borrowing from banks against public securities. The Bombay Act, under

section 106, provides for borrowings from Central or State Governments or others too.

- (5) Section 153 of the Calcutta Act provides for borrowing from the State Government only, and attachment of the Municipal Fund for recovery of such money.
- (6) Section 140 of the Calcutta Act refers to the form and effect of debentures whereas section 118 of the Gujarat Act refers to form of debentures only.

The Madhya Pradesh Act, under sections 105, 106 and 107 specifies the form, exchange, transfer and effect of debentures, signature on coupons attached to debentures, and for issuing debentures to two or more persons jointly.

Section 109 of the Madhya Pradesh Act, section 122 of the Gujarat Act and section 110AA of the Bombay Act relate to the renewal of debentures and section 110 of the Madhya Pradesh Act, section 123 of the Gujarat Act and section 110AC of the Bombay Act cover the liabilities in respect of the debentures renewed.

- (7) Various sections in the laws provide for establishment, maintenance and application of *Sinking Funds* for loans, such as under sections 145 and 150 of the Calcutta Act, sections 114 and 118 of the Madhya Pradesh Act, and section 112 of the Gujarat Act.

Other sections provide for investment of Sinking Fund (section 147 of the Calcutta Act, section 109A of the Bombay Act, section 116 of the Madhya Pradesh Act and sections 113 and 114 of the Gujarat Act).

Section 154 of the Calcutta Act and section 122 of the Madhya Pradesh Act provide for *Attachment of Municipal Fund for Securing Payments into Sinking Funds*.

Section 109AA of the Bombay Act, section 115 of the Gujarat Act, section 120 of the Madhya Pradesh Act and section 152 of the Calcutta Act provide for *annual examination of the Sinking Funds*.

- (8) In the present context, it is desirable to make provisions in the law for the roles which may be performed by the credit rating agencies.
- (9) The legal issues considered in assessing the debt-bearing capacity cover factors like provisions for creation of debt-servicing funds and the legal procedures for seeking

recourse in the event of default. Other legal considerations include the ability of the municipal entity to pledge revenues for debt-servicing and extend collateral in terms of commercial property, plant and machinery and other assets. The administrative capacity of the municipal entity is assessed in terms of tax-collection abilities and experience in managing arrears in collections. In addition, the technical ability to operate urban infrastructure facilities is also assessed.

- (10) Of late, there are number of examples relating to the development of the municipal bond market in India as highlighted, yearwise, in the March 2001 issue of Urban Finance (Volume 4, No.1) published by the National Institute of Urban Affairs under the Indo-USAID Project on Financial Institutions Reform and Expansion (FIRE-D) Project supported by the United States Agency for International Development (USAID) (see *Annex 4*).

Provisions Made in the Municipal Law

25. *In the first place, the Municipal Law has made a provision for framing by the State Government of a Comprehensive Debt Limitation Policy applicable in case of loans to be raised by the Municipalities, laying down, inter-alia, the general principles governing the raising of loans, the limit of loans which any Municipality may raise having regard to its financial capacity, the rate of interest to be paid for such loans and the terms and conditions including the period of repayment thereof.*

26. *The Municipal Law further provides for the following :*

<u>Clause Number</u>	<u>Marginal Title</u>
109	<i>Power of Municipality to raise loan</i>
110	<i>Power of Municipality to open credit account with bank</i>
111	<i>Power of Municipality to raise short-term loan</i>
112	<i>Establishment of Sinking Fund</i>
113	<i>Application of Sinking Fund</i>
114	<i>Power to discontinue payment towards Sinking Fund</i>
115	<i>Investment of amount at the credit of Sinking Fund</i>
116	<i>Power of Municipality to reserve a portion of debentures, issued for raising loan, for investment</i>

117	<i>Manner of repayment of loans</i>
118	<i>Form and effect of debentures</i>
119	<i>Annual statement</i>
120	<i>Annual examination of Sinking Funds</i>
121	<i>Power of Municipality to borrow money from State Government and attachment of Municipal Fund for recovery of such money</i>
122	<i>Issue of Municipal Bonds for development of urban infrastructure</i>
123	<i>Credit Rating of Municipal Bonds</i>
124	<i>Pledging of municipal assets as security for Municipal Bonds</i>
125	<i>Debt Service Reserve Fund</i>
126	<i>Limit to encumbrances through future debt</i>
127	<i>Use of proceeds from Municipal Bonds</i>