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EDITORIAL

“In a world that is naturally geared towards acquiring certainties, it is by no means obvious that doubt is the inevitable companion of the researcher, whatever his or her discipline. All the more so in a discipline like law in which the notion of authority is so powerful and ingrained in our mind.”

- Andrea Bianchi, An Inquiry into Different Ways of Thinking

A foundational principle of any functional legal system is the presumption of a single, objective reality. Judges, in part, are tasked with authoritatively discerning this reality from competing interpretations. However, law has multiple audiences that it speaks to, and this adopted reality is constrained by the questions we choose to ask or avoid and the boundaries we draw in framing those questions. As Bachelard reminds us, the knowledge we construct is shaped by “*epistemological obstacles*”—changes, or rather realities, we are unwilling to accept or even see. In this ecosystem, scholars play their role by asking new questions and illuminating new ways of seeing, enabling us to construct richer, more inclusive realities of what is possible in law and beyond. This is the purpose that this Journal, like many others, aspires to serve.

The articles in this edition remind us that asking better questions can lead to better answers. From the long-standing conflict in Nagorno-Karabakh to the need for insolvency laws for municipalities, they tackle pressing issues with fresh perspectives. Whether it’s rethinking gig workers’ safety, judicial performance or balancing rights like free speech and privacy, each piece challenges us to see the law not just as it is but as it could be.

This ethos of curiosity and openness has guided the work of this Board. Over the past months, we have reflected deeply on what it means to be an editor and how to engage with submissions in thoughtful and meaningful ways that genuinely add value. Moving away from a test-based evaluation system, we adopted a continuous evaluation process for the promotion test, introduced more flexibility in subject area choices for reviewers, and set new ambitious targets that the Journal can strive towards.

With that, we proudly present the first issue of the nineteenth volume of this Journal. I express my heartfelt gratitude to our authors, whose thoughtful contributions form the heart of this edition; to the editors, whose inspiring dedication and sincerity have guided every step and detail of this process; to Hari Sir for his unwavering support; to Anil Sir for his invaluable guidance; and to our faculty advisors, whose thoughtful suggestions have greatly enriched the editorial process.

On behalf of the Board of Editors,

Fathima Rena Abdulla,

Editor-in-Chief

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India Should Introduce an Insolvency Law for the Municipalities and Local Bodies

Devendra Mehta *

Abstract

Municipalities have to undertake massive capital expenditure to build infrastructure and fulfil their obligations to the citizens as envisaged in the Constitution. However, they are faced with dwindling revenues, high administrative expenses, deteriorating credit profiles, borrowing restrictions, and conditionalities on receipt of the grants. As a result, municipalities need to find novel methods to enhance their revenue-generating and fund-raising capabilities. Introducing legislation for the insolvency of municipalities and similar local bodies will help spur infrastructure financing. Though the Constitution will determine the bounds of such an insolvency law, an insolvency law will bring transparency, mitigate risk, lower borrowing costs, garner a wider pool of capital, delineate principles between public interest and creditor rights, and signal to lenders that debt restructurings will be predictable. Additionally, certain novel methods, which are currently sparsely used, may see wider usage by municipalities to bolster their financial position on introducing such a law. Concurrently, numerous best practices and precedents established in the corporate insolvency resolution process can be transitioned into a municipal insolvency law, enabling a smoother implementation.

I. Background

Village Panchayats, the rural local governing bodies, have been functioning in India since ancient times and have continued to be in existence under the

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Mughals and the British, in some guise. The urban local bodies have been in existence for two hundred years. The Municipal Corporation of Chennai (Madras) was set up in 1688, and that of Kolkata (Calcutta) and Mumbai (Bombay) in 1726.¹

Post-independence, the assimilation of local governing bodies, the third tier, in the mainstream government was initiated with the enactment of the Seventy-Third and Seventy-Fourth Amendments to the Constitution; Part IX, consisting of Articles 243 to 243O pertains to The Panchayats and Part IXA, consisting of Articles 243P to 243ZG deal with The Municipalities.²

This paper primarily deals with The Municipalities³ (“TMs”). Article 243W, in conjunction with the Twelfth Schedule of the Constitution, delineates eighteen functions/duties that a State Government may assign to TMs. These functions, apart from public duty, may also have the potential to generate revenue for TMs: land use and construction of buildings, management of roads and bridges, water supply, solid waste management, and urban amenities, etc. In consonance with the aforesaid functions, vide Article 243X, the State may authorise and/or assign TMs to levy, collect or appropriate taxes, duties, tolls, and fees. In addition, the Constitution also provides that the Finance Commission (“FC”) should review the financial position of TMs, an aspect briefly discussed later in the paper. However, the duties and the funding required to perform those duties have not marched in tandem, the latter

¹ Snehashish Mishra & Nilanjan Gupta, *Netaji's mayoral tenure: People-centric administration through nationalistic ethos*, ORF (Jan. 24, 2024), <https://www.orfonline.org/expert-speak/netaji-s-mayoral-tenure-people-centric-administration-through-nationalistic-ethos>.

² INDIA CONST.

³ *Id*; The Municipalities include Nagar Panchayat, Municipal Council and Municipal Corporation as defined in Article 243Q of the Indian Constitution. The definition excludes Cantonment Boards on grounds of national security. Furthermore, the rural urban bodies have been kept out of the purview of the paper.

perpetually falling short. Out of the 18 functions to be performed by municipal bodies, less than half have a corresponding financing source.⁴ Prudent financial principles require that every line item of expenditure should be backed by its revenue stream. Revenue could be either by TMs own revenue or by Central/State grants. In the absence of matching revenue, paucity of funds leads to sub-standard services and poor infrastructure for the populace at a time of growing urbanisation.

II. The Municipalities and Urbanisation

India has been urbanising rapidly on the back of a growing economy wherein the population is transitioning out of the farmlands. Numerous methodologies and classification systems are in existence to define urbanisation: the census criterion, metropolitan regions, urban agglomeration, megapolis, metropolitan city etc. Irrespective of the classification one adopts, at the very minimum, one-third of India's population is urban and is expected to increase to 43% by 2035.⁵

From a governance perspective, a Nagar Panchayat is for the areas transitioning from rural to urban, a Municipal Council is for a small urban area, and a Municipal Corporation is for a large urban area.

The absolute numbers of urbanisation are often understated due to political resistance. *“Often the rural local governments themselves are reluctant to go urban because local politicians are apprehensive that they would not have*

⁴ Reserve Bank of India, *Report on Municipal Finances* (2022), <https://m.rbi.org.in/scripts/PublicationsView.aspx?id=21357>.

⁵ United Nations Human Settlements Programme (UN-Habitat), *World Cities Report 22 – Envisaging the future of cities* (2022), <https://digitallibrary.un.org/record/3984713?ln=en&v=pdf>.

access to large amounts of funds for rural development schemes; they also fear regulations which urbanisation brings with it.”⁶

It is a truism that the development of urban infrastructure in India has not kept pace with urbanisation. The need will further aggravate as the existing infrastructure deteriorates or requires rebuilding due to adverse climatic events like rising sea levels, floods, heat islands, and sandstorms. To cater to the infrastructure needs, the TMs need to enhance their revenue-generating and fund-raising capabilities in conjunction with capacity building and institutional support from the State and the Central Government.

III. State of Municipal Finance in India

Municipal revenues in India from own sources, consisting primarily of property tax, water tax, and toll tax, have been low, at 0.43% of Gross Domestic Product (“GDP”), and the total municipal revenues/expenditures have stagnated at around 1% of GDP for over a decade. In contrast, municipal revenues/expenditures account for 4.5% for Poland, 6% for South Africa, 7.4% for Brazil, 13.9% for the United Kingdom and 14.2% for Norway.⁷

The composition of municipal revenues varies across countries in accordance with their respective constitutions. Local governments in Australia, Belgium, Canada, France, New Zealand, Spain and Switzerland largely depend on their own revenue, whereas the ones in Austria, Greece, Ireland, Luxembourg, Turkey and the United Kingdom rely on general government grants.⁸

⁶ Isher Judge Ahluwalia et al, *State of Municipal Finances in India – A study prepared for the Fifteenth Finance Commission 1* (2019), https://fincomindia.nic.in/archive/writereaddata/html_en_files/fincom15/StudyReports/State%20of%20Municipal%20Finances%20in%20India.pdf.

⁷ *Id.* at 7.

⁸ Reserve Bank of India, *Report on Municipal Finances 12* (2022), <https://m.rbi.org.in/scripts/AnnualPublications.aspx?head=Report%20on%20Municipal%20Finances>.

Ease and efficiency of business dictate that certain taxes like income taxes and value-added taxes should be levied centrally. The latter, in all situations, will result in some loss to the local exchequer and similar was the case with the introduction of Goods and Services Tax (“GST”) in India. However, one solution to obviate such situations is to work out a distribution mechanism from the Central pool to the local authorities based on some preset criterion, for e.g., population, area or any country-specific appropriate metric.

A. Goods and Services Tax was detrimental to Municipal Finance

The revenue-generating capacity of TMs in India has suffered with the introduction of GST. Local and consumption taxes like octroi,⁹ local body tax, entry tax and advertisement tax, which were the prerogative of TMs, have been subsumed within the GST. To make matters worse, the proceeds of GST are divided between the Centre and the State with no constitutional provision providing for sharing with the third tier i.e., TMs. In contrast, many countries across the world have provided for sharing such taxes with their urban local bodies.¹⁰ For example, Brazil shares its tax revenues between its 25 states, the federal district and 5,500 municipalities. Similarly, South Africa also shares an equitable share of nationally raised revenues with its local government.

In India, property tax, accounting for approximately half of tax revenues, is the primary source of revenue.¹¹ Limited revenue sources increase the

⁹ Maharashtra Goods and Services Tax (Compensation to the Local Authorities) Act, 2017, Maharashtra Act No. 41, 2017 provides for compensation on account of octroi to all 27 municipal corporations in Maharashtra. A few other states too have taken some measures but none as robust as that of Maharashtra.

¹⁰ Ahluwalia, *supra* note 6, at 4.

¹¹ Reserve Bank of India, *Report on Municipal Finances* 12 (2022)

<https://m.rbi.org.in/scripts/AnnualPublications.aspx?head=Report%20on%20Municipal%20Finances>.

dependence of TMs on the transfer of funds from the upper tiers, i.e., the State and the Central Government (30% - 35% of revenue receipts), resulting in a lack of financial autonomy.¹² Further, these transfers are not with regular periodicity but are based on the whims and fancy of the State Government. Moreover, Members of the Legislative Assembly (“MLA”) possibly favour erratic transfers, if at all, to showcase their power.

Thus, TMs not only have to claw back the revenue lost but also improve the efficiency of existing revenue streams to reduce dependency on transfers. In addition, TMs should find incremental sources of revenue and funds to provide requisite services.

B. Archaic Laws and Conventions govern Municipal Finance

TMs in India are required to balance their budget by law; indirectly creating a ceiling on the expenditure. Also, TMs treat all expenditures as similar, irrespective of the nature of expense; revenue, or capital.¹³ This antiquated accounting convention needs to change considering the capex requirements of infrastructure that needs to be built. Further, most TMs cannot borrow without the permission of the respective State governments, which in turn may prescribe conditions on the types of instruments, limits, and tenors of repayment;¹⁴ a handful of States have rolled out a policy within which TMs are allowed to borrow.

Municipal borrowings in India are concentrated at a few large corporations and are negligible at less than 0.05 per cent of GDP cumulatively for all TMs. More than half of the borrowings are from banks, financial institutions, and

¹² *Id.*

¹³ Ahluwalia, *supra* note 6, at 5.

¹⁴ Reserve Bank of India, *supra* note 11.

loans from Centre/State governments. Capital markets bond issuances are less than a tenth of the total borrowings, of which the majority has been used for capital expenditure.¹⁵ Bonds of 14 municipalities are listed on Stock Exchanges: Pune, Greater Hyderabad, Ahmedabad, Surat, Indore, Lucknow, and a few others.

A study of 37 large municipal corporations revealed that revenue expenditure was 63% of total expenditure. Within revenue expenditure, administrative expenses accounted for 57%.¹⁶ Thus, the TMs do not have the requisite capacity for the much-needed capital expenditure. Further, deteriorating revenue in conjunction with high administrative expenses leads to an adverse credit profile, making it difficult for TMs to borrow.

The abolition of the Planning Commission also resulted in a gap on account of capital expenditure, as the same was earlier a plan outlay.¹⁷

Thus, a suitable mechanism needs to be devised that makes it attractive for lenders to lend, against requisite security, to TMs. This will enable TMs to fulfil their obligations to citizens in the face of insurmountable odds.

C. Other impediments to Municipal Finance

Competitive electoral politics has been responsible for the deteriorating fiscal position of the States, and the situation may worsen further. The adverse fiscal position will make it increasingly difficult for the States to allot additional funds to TMs. Moreover, a hike in property tax rates or user charges for

¹⁵ *Id.*

¹⁶ Ayush Khare et al., *Finances of Municipal Corporations in Metropolitan Cities of India – A study prepared for the Fifteenth Finance Commission 21* (2019), <https://fincomindia.nic.in/asset/doc/commission-reports/15th-FC/reports/studies/Finances%20of%20Municipal%20Corporations%20in%20Metropolitan%20cities%20of%20India.pdf>.

¹⁷ Ahluwalia, *supra* note 6, at 5.

services provided by TMs is also frowned upon by politicians, even though the property values, as recorded by the TMs, are always lagging behind the market value. A study of the six largest municipalities revealed that TMs faced challenges in aligning the value of properties to market and levy tax accordingly.¹⁸ Also, an increase in user charges requires the permission of the State, which is loath to grant the same due to public opposition.¹⁹ The aforesaid low base gets further eroded in case of a poor macro-economic environment; Brihanmumbai Municipal Corporation's ("BMC") property tax collection for the fiscal year 2023-24 at INR 32 Bn was substantially below its target of INR 45 Bn.²⁰

In addition, TMs give several exemptions to religious and charitable institutions, public properties, educational institutions, senior citizens etc. Central Government properties too are exempt from municipal taxes.²¹ Furthermore, the freedom to realise better revenue through unlocking property value is restricted. For example, a higher FSI in Mumbai will yield higher property taxes, but the power to increase FSI vests with the State Government.²² All of the above create challenges for TMs to enhance revenue. Kyoto, a city in Japan, which was on the verge of bankruptcy is an example wherein similar problems were encountered and provides a partial template for the likely solutions.

Kyoto's temples and shrines, which are legally registered religious corporations, are exempt from property taxes. To preserve the city's traditional

¹⁸ Khare, *supra* note 16, at 25.

¹⁹ *Id.* at 13.

²⁰ Richa Pinto, *At ₹3k cr, BMC records lowest property tax mop up in 10 years*, TIMES OF INDIA (Apr. 2, 2024), <https://timesofindia.indiatimes.com/city/mumbai/at-rs-3k-crore-bmc-records-lowest-property-tax-mop-up-in-10-years/articleshow/108960561.cms>.

²¹ Khare, *supra* note 13, at 27.

²² *Id.* at 33.

atmosphere, the height of buildings is limited, resulting in lower property taxes. Also, due to demographics, some residents pay low or no property tax; 10% of Kyoto's residents are college students, and about 28% of residents are over 65.²³ In addition, the city took on some projects which never achieved the forecasted revenues, primarily the Tozai subway line;²⁴ an aspect discussed later in the paper vis-à-vis China.

Kyoto thus had to prepare a restructuring plan that called for trimming the bureaucracy, raising the minimum age of those eligible for discounts, and cutting subsidies.

Rio de Janeiro in Brazil declared a State of public calamity²⁵ in 2016, the primary reason being the decrease in tax collection, especially regarding goods, services, royalties, and special interests in oil. One of the reasons for the decrease was excessive tax incentives.²⁶ This again demonstrates that too many tax incentives may be popular in the short run but are disastrous for fiscal health in the long run.

D. Role of Finance Commissions in Municipal Finance

Article 280(c) of the Constitution casts a duty on the Finance Commission to recommend measures needed to augment the Consolidated Fund of a State to supplement the resources of TMs.²⁷

²³ Eric Johnston, *Kyoto is facing bankruptcy. What happens now?*, THE JAPAN TIMES (Sep. 21, 2021), <https://www.japantimes.co.jp/news/2021/09/20/business/kyoto-bankruptcy-tourism/>.

²⁴ Lucy Kraft, *Kyoto, Japan's beautiful imperial capital, is going broke fast*, CBS NEWS (May 20, 2022), <https://www.cbsnews.com/news/japan-kyoto-tourism-city-faces-bankruptcy/>.

²⁵ Abnormal situation arising due to disasters, damages or losses resulting in postponement of payment of debt instalments, expenses etc.

²⁶ Catarina Ferraz, *When liquidation is not an option: A global study on the treatment of local public entities in distress* (Nov. 2022) (academic paper, INSOL International) (on file with Royal Holloway, University of London).

²⁷ INDIA CONST., art. 280(c).

Six Finance Commissions, from FC-X to FC-XV, have given their recommendations for local bodies. The grants for urban local bodies have increased from INR 1,000 crores of FC-X to INR 87,144 crores of FC-XIV, though the actual disbursements were 10% to 18% lower due to failure of local bodies to meet the conditionalities.²⁸ FC-XV has recommended a total grant of INR 1,21,055 crores.

The conditionalities prescribed for grants have varied from year to year. FC-X and FC-XI required that no grant amount was to be used for expenditure on salaries and wages. In addition, FC-XI suggested the usage of grants for the maintenance of accounts and audits, development of a financial database and balance for maintenance of core services like primary education, health care, safe drinking water, sanitation, etc.

The FC-XII recommended that priority be given to the creation of financial databases and maintenance of accounts using modern technology and management systems. Further, 50% of the grant should be used for solid waste management.²⁹

The FC-XIII stipulated nine conditions to access 33% of the grants. These conditions primarily pertained to accounts, audits, budget documents, electronic banking, State finance commissions, property tax and delivery standards for essential services.

The FC-XIV recommended grants in two parts: an unconditional basic grant and a 20% conditional performance grant. The conditional performance grant required local governments to show an increase in their own source of revenue

²⁸ XV Finance Commission, *Finance Commission in Covid Times – Report for 2021 – 26* 172 (2020), <https://fincomindia.nic.in/asset/doc/commission-reports/XVFC%20VOL%20I%20Main%20Report.pdf>.

²⁹ Ahluwalia, *supra* note 6, at 22.

and submit audited annual accounts. Municipalities, in addition, had to publish the service level benchmarks relating to basic urban services each year.

The FC-XV prescribed minimum entry-level conditions for the grants, web-based availability of annual accounts for the previous year and audited accounts for the year before as well as notification of minimum floor rates of property taxes. In addition, for million-plus cities, about 32% was tied to ambient air quality standards, and the remaining to meet service level benchmarks on drinking water supply, rainwater harvesting, water recycling, solid waste management and sanitation. For non-million-plus cities, 40 per cent of the grants are untied, and 60 per cent is tied to the national priorities of drinking water, rainwater harvesting, solid waste management and sanitation.

The common threads that run through the recommendations of finance commissions are that of more robust accounts, timely audits and meeting the service level benchmarks for essential services, all improving over the years, but not yet satisfactory. The importance can be seen from the fact that the Constitution, too, under Article 243Z, states that the State must make provision with respect to maintenance of accounts of municipalities and the auditing of such accounts.

E. The Way Forward for Municipal Finance

As articulated above, TMs must undertake massive capital expenditure to provide the services as provided in the Constitution but are faced with dwindling revenues, high administrative expenses, deteriorating credit profile, borrowing restrictions, conditionalities on grants of finance commission and the arduous task of balancing the budgets.

FC-XV has suggested more efficient property tax administration and rationalisation of professional tax to improve revenue. In addition, all levels of government should jointly explore the introduction of three three-tiered

GST. Moreover, TMs should have an unfettered right to vehicle taxes, parking taxes, green surcharges, local entertainment tax, land-based taxes, and unlocking of land value, including FSI, to augment municipal revenues.

As the examples of Kyoto and Rio illustrate, inefficiencies of revenue are a potential hazard for the long term. A similar fate awaits several municipalities/cities/councils in the United Kingdom. One in ten councils in England have warned that they will go bankrupt in the next twelve months.³⁰ Councils are handling the financial distress as befits them; Thurrock, Slough, Croydon, and Birmingham have raised local taxes by 10%,³¹ Nottingham intends to raise prices of events, public toilets, and transport;³² Middlesbrough voted for maximum tax rise along with a charge for green waste;³³ Birmingham is dimming streetlights, resorting to less frequent waste collection and stopping expenditure on arts.³⁴ Across England, libraries, museums, leisure centres and parks are bracing for cuts.³⁵

Thus, the municipalities must strike a fine balance of revenue enhancement without inconveniencing its populace; a stitch in time saves nine.

³⁰ Patrick Butler, *Nearly one in 10 English councils expect to go bust in next year, survey finds*, THE GUARDIAN (Feb. 28, 2024), <https://www.theguardian.com/society/2024/feb/28/nearly-one-in-10-english-councils-expect-to-go-bust-in-next-year-survey-finds>.

³¹ Eugenio Vaccari & Yselt Marique, *One in five councils at risk of bankruptcy – what happens after local authorities run out of money*, THE CONVERSATION (Feb. 14, 2024), <https://theconversation.com/one-in-five-councils-at-risk-of-bankruptcy-what-happens-after-local-authorities-run-out-of-money-222541>.

³² *Id.*

³³ Naomi Corrigan, *Council budget to avoid bankruptcy approved*, BBC NEWS (Mar. 10, 2024), <https://www.bbc.com/news/articles/cm5ry0v0190o>.

³⁴ Tom Rees, *UK Town's are going Bankrupt. Here's what's gone wrong*, BLOOMBERG (Feb. 28, 2024), <https://www.bloomberg.com/news/articles/2024-02-28/uk-towns-are-going-bankrupt-here-s-what-s-gone-wrong-quicktake>.

³⁵ Open Access Government, *Local government's financial crisis: Are local institutions disappearing?* (Jan. 17, 2024), available at <https://www.openaccessgovernment.org/local-governments-financial-crisis-are-local-institutions-disappearing/172428/>.

Whilst the revenue enhancement mechanisms will take care of revenue expenditure and contribute partly to infrastructure enhancement, the States should liberalise borrowing thresholds for TMs for the capital projects, with appropriate caps and within defined financial ratios. Caps, ratios, and vigil on off-balance sheet borrowing, a prerequisite to avoid situations like that of China, are described later in the paper. Borrowings within the bounds of rationality will ensure that the creation of new infrastructure is not hindered due to lack of funds. Certain provinces in Canada, like Ontario, Quebec, Manitoba, and Prince Edward Island, allow municipalities to borrow only for capital projects, albeit with caps.³⁶

Also, several large cities are being constructed across the globe, vying for the same pool of limited finance; ninety-one cities have been announced in the past decade, of which fifteen in the last year.³⁷

This paper argues that the introduction of legislation for the insolvency of TMs will not only spur financing for the aforesaid infrastructure but also will bring about improvements in the conditions imposed by finance commissions, which in turn will bring transparency. The paper would rely on experience and concepts of other jurisdictions where applicable. An endeavour would be made to keep the law practical; the best model law is of little use if it is not implementable, as is usually talked about in the South African municipal insolvency law. The paper starts by answering the question, why an insolvency law?

³⁶ Stephanie Ben-Ishai, *Local public entities in distress – a critical analysis of the Canadian approach* (Nov. 2022) (academic paper, INSOL International) (on file with Royal Holloway, University of London).

³⁷ *Boom: towns, why everyone is building new cities*, THE ECONOMIST, (Mar. 7, 2024), <https://www.economist.com/finance-and-economics/2024/03/07/the-world-is-in-the-midst-of-a-city-building-boom>

IV. Why an Insolvency Law for Municipalities?

Port Canning Municipality (“PCM”), established in 1862,³⁸ is the first and possibly the only municipality that went bankrupt in India. The municipality had grand plans for parks, wharves, jetties, tramways, railway stations, and dockyards which didn’t materialise.

The origins of PCM are interesting. In 1853,³⁹ the Bengal Chamber of Commerce (“BCC”) feared that the silting of the Hooghly River might result in Calcutta Port becoming unnavigable, and a search for an auxiliary port ensued. Matla estuary,⁴⁰ 45 km south-east of Calcutta, amongst Sunderbans, was chosen where the waters of Bidyádhari, Karatoyá, and Athárabánká rivers converged. Henry Piddington,⁴¹ a storm expert, warned that the site is unsuitable for a port as a cyclone may destroy the port. Nevertheless, about 9000 acres of land were acquired: 8260 acres in the first instance⁴² and 650 acres in the second.⁴³ The port was named after then-Governor General Charles Canning, who subsequently became the Viceroy. The municipality had taken loans and issued debentures worth INR 1 Mn.⁴⁴ A railway line from Calcutta to Port Canning was built for INR 6M.⁴⁵ A company, Port Canning Land Investment, Reclamation and Dock Company (“PCC”), was incorporated to undertake work essential to the port with exclusive concessions and rights. PCC thereafter issued equity, which had a premium of

³⁸ F.E. Pragiter, *Cameos of Indian Districts – The Sunderbans*, 89 THE CALCUTTA REVIEW 280, 295 (1889).

³⁹ *Id.*, at 294.

⁴⁰ W.W. HUNTER, THE IMPERIAL GAZETTEER OF INDIA, XI 216 (1886).

⁴¹ Amitav Ghosh, *Remembering Henry Piddington, Meteorologist Extraordinaire, And His Prophetic Warnings*, READER’S DIGEST (May 23, 2020).

⁴² Pragiter, *supra* note 38, at 294.

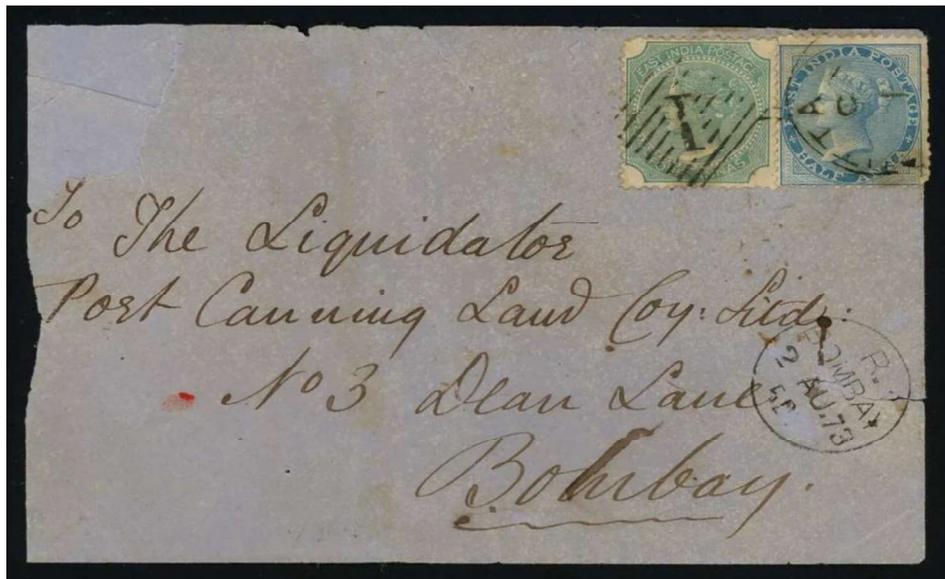
⁴³ HUNTER, *supra* note 40, at 217.

⁴⁴ JOHN BESEMERES, PORT CANNING PROBLEM; A LETTER TO THE RIGHT HON. LORD STANLEY, M.P., REVISED AND REPRINTED FROM THE INDIAN EXAMINER 5 (1868).

⁴⁵ *Id.*

INR 12,000 in Bombay and INR 10,000 in Calcutta.⁴⁶ A number of reasons made the port unviable, and the final nail was a cyclone on November 2, 1867, which destroyed the port.

PCC was put into liquidation in 1870, and PCM faced bankruptcy; suits were instituted by debenture holders, property of the municipality was attached against a decree, debentures were commuted for freehold land rights, some were paid at 50% of value, and the Government declared that it had no obligation to fulfil the liability. The whole of Canning municipal estate was attached and put under the charge of the Collector.⁴⁷



An 1873 envelope addressed to The Liquidator of the Port Canning Company

One hundred fifty years have passed since the Port Canning bankruptcy, but

⁴⁶ HUNTER, *supra* note 40, at 217.

⁴⁷ *Id.* at 219.

we still await a law on municipal insolvency. Friedrich Meili, a renowned Swiss law professor, put forward a detailed proposal for a law when four municipalities were on the brink of insolvency in Switzerland. He stated that the main benefit of such a law is that of legal certainty.⁴⁸

The legal certainty arising out of the Insolvency and Bankruptcy Code (“IBC”) is one of the reasons that has resulted in the phenomenal growth of private credit. Similarly, municipal insolvency laws, in the first instance, will act as a signalling exercise to lenders that debt restructurings will be predictable and equitable. Though a lack of insolvency law is not the only factor inhibiting lenders, it is an important one, in conjunction with the lack of robust accounts, as pointed out by various Finance Commissions, FC-XI to FC-XV, have been vociferous over the lack of accounts and have reiterated the fact in every report. In contrast to lenders, the law will signal to TMs that whilst they must maintain essential services, fiscal profligacy will have consequences.

Importantly, such laws also help to achieve macroeconomic goals. Effective insolvency laws and creditor rights systems lead to efficient capital markets, better risk management, lower borrowing costs, and availability of a wider pool of capital for credit; in effect minimizing systemic risk. This in turn, expands the fiscal space for infrastructure investments, promotes fiscal transparency, and deepens financial market reforms.⁴⁹

In a circuitous way, capital markets help municipalities improve upon the deficiencies pointed out by the Finance Commissions. Guwahati Municipal

⁴⁸ Lili Liu & Michael Waibel, *Subnational Insolvency: Cross Country Experience and Lessons* 22 (Working Paper, Policy Research Working Paper) 4496 (2008). https://papers.ssrn.com/sol3/papers.cfm?abstract_id=1400640.

⁴⁹ *Id.* at 33.

Corporation is adopting double-entry bookkeeping to access the capital markets.⁵⁰

Good infrastructure will improve productivity in the economy and help India grow faster. On the flip side, bereft of good infrastructure, the cities over a period will start to decline as no one would want to stay in them. A recent example of a reaction to poor infrastructure is from the city of Bangalore, where people are contemplating a move out of the city due to water shortage. Similarly, the post-Covid world showed us glimpses of such an eventuality as the employees were reluctant to return to cities because of poor infrastructure: overcrowded buildings, congested roads, inadequate open spaces, sluggish progress of metro, increased commute times due to traffic congestion, reduced family time, soaring rents and increased cost of living.⁵¹ It is true that most employees will return, given the current state of the job market. However, if such an eventuality takes place at any time in the future in a better macro environment, the prices of properties will start to decline, with a concomitant effect on the revenues of TMs.

Thus, the introduction of municipal law will help kick-start investments in urban infrastructure by giving confidence to lenders to lend at the risk adjusted borrowing costs. Further, in the eventuality of an insolvency, the laws will give confidence to creditors of structured equitable resolution, enabling TMs to re-enter capital markets.⁵² Simultaneously, TMs are put on a sustainable path to deliver public services post-resolution.

⁵⁰ *Climate change mitigation needs funding*, THE INDIAN EXPRESS (Sep. 13, 2024), <https://indianexpress.com/article/india/climate-change-mitigation-needs-funding-9564785/>.

⁵¹ Ashish Kolvalker, *Why a complete return to office may not be the best approach for India Inc.*, PEOPLE MATTERS (Jul. 6, 2023), <https://www.peoplesmatters.in/article/employee-relations/why-a-complete-return-to-office-may-not-be-the-best-approach-for-india-inc-38339>.

⁵² Liu & Waibel, *supra* note 48, at 4.

However, before we embark on the nuances of municipal insolvency law, a brief overview of the peculiarities of TMs is essential.

V. **Peculiar Characteristics of Municipalities in India**

The boundaries of an insolvency law for municipalities are set by the Constitution. Article 243Q⁵³ specifies the modus operandi for constituting TMs, and Article 243R⁵⁴ mandates that the persons forming part of the TMs are to be chosen by direct elections.

In addition, the State may, by law, provide representation of persons having special knowledge or experience in municipal administration. Also, the State may, by law under Article 243X,⁵⁵ authorise TMs to levy, collect and appropriate taxes, duties, tolls, and fees.

As mentioned above, TMs are responsible for eighteen essential duties prescribed under Article 243W⁵⁶ read with the Twelfth Schedule⁵⁷ like urban planning, regulating land use and construction, water supply, health and sanitation, fire services, protection of the environment, urban poverty alleviation, slum upgradation etc. Though not specified in the Constitution or the State laws, whilst providing essential services, TMs may or may not charge a fair price, i.e., the cost of providing the services. Currently, the user charges vary across municipalities; at the lower end 8% of revenue expenditure for Chennai and 17% for Kolkata, whereas a high of 82% for Bangalore.⁵⁸

Supreme Court, in the case of Hindustan Construction Company,⁵⁹ while

⁵³ INDIAN CONST., art. 243Q.

⁵⁴ INDIAN CONST., art. 243R.

⁵⁵ INDIAN CONST., art. 243X.

⁵⁶ INDIAN CONST., art. 243W.

⁵⁷ INDIAN CONST., Schedule XII.

⁵⁸ Khare, *supra* note 16, at 31.

⁵⁹ Hindustan Construction Company Limited & Anr. vs. Union of India & Ors, (2019) SCC OnLine SC 1706.

referring to NHAI, had said that the development and maintenance of national highways is a government function that falls within Entry 23 of List I of the Seventh Schedule⁶⁰ to the Constitution of India. It further added that “*NHAI is a statutory body which functions as an extended limb of the Central Government and performs governmental functions which obviously cannot be taken over by a resolution professional under the Insolvency Code, or by any other corporate body. Nor can such Authority ultimately be wound up under the Insolvency Code.*” Partially, a similar reasoning may apply to TMs as per se they cannot be liquidated.

Thus, a successful resolution/restructuring must be the outcome of insolvency; in-effect, a debtor-in-possession restructuring with an independent oversight. However, this paper also delves into “*municipality-like*” Public Private Partnership (“PPP”) that may be amenable to liquidation in limited circumstances.

Also, strictly applying the aforesaid judgement may imply that a resolution professional may not be able to take over the management of TMs. However, as discussed later in the paper, based on current practice in TMs and the fact that TMs are fundamentally different from central statutory bodies, it is possible to take over the management of TMs by a resolution professional if the person simultaneously works under the directions of the State. Thus, a takeover of management, though not possible under IBC, is possible under a municipal insolvency law.

VI. Building Blocks of an Insolvency Law for Municipalities

INSOL International published a study on local entities in distress in 2022, recommending broad contours of insolvency law for such entities. The study

⁶⁰ INDIAN CONST., Schedule VII.

acknowledged the fact that laws pertaining to local public entities in distress are heavily influenced by local traditions, cultures, and history. There is no one-size-fits-all approach, and encouraged national legislators to devise principles based on their unique circumstances.⁶¹

Nevertheless, the study advocated that “*in determining the rules applicable to local public entities in distress, domestic legislators should pursue territorial solutions based on the uniform, traditional principles of collectivity and equality of treatment of creditors.*” Furthermore, the law should be predictable, fair, transparent and allow the participation of all parties in the process to safeguard their respective interests.

In several other jurisdictions, the local entities are in distress because of growing demand from an aging and declining population resulting in dwindling revenues. However, India is not in the same economic cycle. India has a growing population, and a robust municipal insolvency law will impart confidence amongst creditors to lend to municipalities for capital expenditure. As explained, in India, the reasons for the decline in revenue are some of the taxes were subsumed into GST, low or no increase in property taxes and user charges, inability to levy new taxes, reluctance on the part of States to cede control over revenue streams and the general inefficiency of TMs.

Moreover, municipalities inherently deal with public interest; an aspect that has been accorded great importance in insolvency laws. Article 6 of the UNCITRAL Model Law on Cross-Border Insolvency specifically carves out an exception that prevents the Court from refusing to take an action if the action would be manifestly contrary to public policy.⁶²

⁶¹ Ferraz, *supra* note 26.

⁶² UNCITRAL, MODEL LAW ON CROSS-BORDER INSOLVENCY GUIDE TO ENACTMENT AND INTERPRETATION 146 (2013).

In accordance with the aforementioned limitations as defined by the Constitution, the public interest involved, and the broad guidelines by INSOL International, let us embark on creating the nuts and bolts of such an insolvency framework.

A. Who should be included in the definition of Municipality?

Nagar Panchayats, Municipal Councils, and Municipal Corporations constitute TMs by definition. In addition, any statutory body arising out of the District Planning Committee under Article 243ZD of the Constitution,⁶³ Metropolitan Planning Committee under Article 243ZE of the Constitution⁶⁴ and similar bodies under any State law should be included in the definition of TMs.

The rationale for the inclusion of Article 243ZD and Article 243ZE is provided by the Constitution, as the two Articles are embodied in Part IXA⁶⁵ of the Constitution, which deals with TMs. *Vis-à-vis* the other bodies that are to be included in the definition of TMs, a two-fold test can act as an appropriate yardstick; firstly, it is a statutory body, and secondly, it is providing any of the services specified in the Twelfth Schedule of the Constitution. An affirmative answer would result in an inclusion. This is because the aforesaid bodies, though in name not municipalities, are performing similar functions. The example of the Yamuna Expressway Industrial Development Authority illustrates this fact.

Jaypee Infratech Limited (“JIL”) was part of the first twelve cases that were referred under IBC. However, the case took long to resolve; it had been

⁶³ INDIAN CONST., art. 243ZD.

⁶⁴ INDIAN CONST., art. 243ZE.

⁶⁵ INDIAN CONST., Part IXA.

meandering through the Courts, with multiple visits to the Supreme Court.⁶⁶ The presence of a municipal insolvency law may have resulted in a quicker resolution.

In brief, the relevant facts of the case are as follows. Yamuna Expressway Industrial Development Authority⁶⁷ (“YEIDA”) was to acquire land from farmers for the development of industrial, commercial and residential areas. In accordance with its mandate, YEIDA signed a lease agreement for the construction of an expressway and commercial exploitation of adjoining land with Jaiprakash Associates Limited, subsequently assigned to JIL. Farmers whose lands were acquired were demanding fair compensation. On orders of the State Government, YEIDA agreed to the demands of the farmers. Meanwhile, JIL was admitted to insolvency. The resolution applicants in insolvency treated compensation payable to YEIDA as an unsecured operational debt and assigned a paltry sum to the claim in their resolution plans; an amount of INR 1 Mn was assigned to YEIDA against its claim on account of additional compensation of INR 16.89 Bn.⁶⁸ YEIDA had consistently been challenging such treatment of its claim by the resolution applicants. Thus, the resolution plan, though approved on March 23, could not be implemented for over a year. The State Government did not consent to the resolution plan of the successful resolution applicant.⁶⁹

⁶⁶ IDBI Bank Limited v. Jaypee Infratech Limited, Company Petition No. (IB)-77(ALD)/2017 of 2023 (NCLT, Allahabad).

⁶⁷ UP Government has enacted the UP Industrial Development Act 1976, to ensure planned development of industrial and allied activities in the State. Yamuna Expressway Industrial Development Authority has been created under this Act for systematic development of notified area abutting Delhi.

⁶⁸ Yamuna Expressway Industrial Development Authority v. Monitoring Committee of Jaypee Infratech Ltd and Suraksha Realty, Company Appeal (AT) (Insolvency) No. 493 of 2023 (NCLAT Delhi).

⁶⁹ *Id.*

YEIDA's role was akin to that of TMs; TMs operate for the benefit of their local municipal area, whereas YEIDA mandate covered a larger geographical footprint; the first duty prescribed under the Twelfth Schedule is that of "*urban planning including town planning*." However, the resolution applicants and the Courts were searching for a solution within the four walls of the CIRP. A municipal insolvency law would have safeguarded the rights of YEIDA as resolution plan applicants would not have treated the debt as an operational debt and assigned the claim a higher value. Eventually, in May 2024, after the successful resolution applicant agreed to pay INR 13.34Bn to YEIDA on account of compensation, did the resolution plan moved forward.⁷⁰ In case the rights of YEIDA would have been protected under a municipal insolvency law, *ab initio*, it is likely that the insolvency would have been resolved faster; litigation by YEIDA may have been avoided. Moreover, it is likely that YEIDA would have accommodated the successful resolution applicant with an additional Floor Space Index ("FSI") to make the project viable.

Similarly, providers of services specified in the Twelfth Schedule in a PPP, irrespective of the corporate structure, should be subjected to the rules of Municipal Insolvency. This is because such service providers, in several cases cannot be liquidated; express consent of the municipality should be sought for such liquidations. The only caveat should be that the legal rights of the municipality, ex-post, should be the same as ex-ante in case of insolvency and restructuring; municipalities' share, whether in equity or in kind, should continue *in toto*. The private service provider should either rejig the debts or a new more efficient service provider should be brought in as in a Corporate Insolvency Resolution Process ("CIRP").

⁷⁰ *Id.*

Mumbai Metro One Private Limited (“MMOPL”) is one such example. State Bank of India, IDBI Bank and Indian Bank had filed separate applications for insolvency against MMOPL for nonpayment of bank dues. Reliance Infrastructure Limited (“RIL”), at the time of filing of insolvency application, was a 74% shareholder, and Mumbai Metropolitan Regional Development Authority (“MMRDA”) held the balance 26%.

The company operates the Versova to Ghatkopar metro line, and the ridership is high. In the case of a CIRP, in the absence of a resolution applicant, the company would undergo liquidation and will inconvenience a lot of passengers. MMRDA was aware of this fact and recently got a valuation done of Reliance Infra’s share to explore the possibility of buying the same. The negotiations between MMOPL and MMRDA have been going on since 2020; MMOPL is claiming a valuation of INR 40.26 Bn, and MMRDA is pegging the same at INR 23.56 Bn.⁷¹ Eventually, the State cabinet allowed MMRDA to purchase an RIL stake for INR 40Bn in March 2024.⁷² This led to the disposal of insolvency applications by the Courts. However, the banks were in a quandary as the cabinet reversed its decision to purchase in June 2024.⁷³ Instead, the cabinet has advised MMRDA to consider a one-time settlement at INR 17Bn.⁷⁴ Bereft of a municipal insolvency law the State has to spend its

⁷¹ Priyanka Kakodkar, *Panel values R-Infra’s 74% stake in Metro-I corridor at 4000 cr*, SUNDAY TIMES OF INDIA (Mar. 10, 2024),

<https://timesofindia.indiatimes.com/city/mumbai/panel-values-r-infras-74-stake-in-metro-1-corridor-at-4000cr/articleshow/108367278.cms>.

⁷² Priyanka Kakodkar, *Cabinet okays buyout of R-Infra stake in Metro-I*, TIMES OF INDIA (Mar. 12, 2024), <https://timesofindia.indiatimes.com/city/mumbai/cabinet-clears-purchase-of-r-infra-stake-in-metro-1-corridor/articleshow/108415038.cms>.

⁷³ Manthan K Mehta, *3 months on, cabinet does U-turn on buyout of R-Infra stake in Metro-I*, TIMES OF INDIA (Jun. 29, 2024) <https://timesofindia.indiatimes.com/city/mumbai/panel-values-r-infras-74-stake-in-metro-1-corridor-at-4000cr/articleshow/108367278.cms>.

⁷⁴ Manthan K Mehta, *State not to buy Metro1 but clear its INR 1.7K cr debt*, TIMES OF INDIA (Jul. 5, 2024).

precious resources on a settlement. A municipal insolvency law would have resulted in the restructuring of the private partner's share.

The case of Seven Hills Hospital,⁷⁵ specifically in the context of the Mumbai hospital,⁷⁶ is another example. In case a municipal insolvency law was in existence, as proposed in this paper, the case may have been resolved by now, which has been in limbo for six years. The proposed resolution plan, in CIRP, had not only impinged on the rights of the Municipal Corporation of Greater Mumbai ("MCGM") by creating a charge for further borrowings but also was overriding MCGM's right and its public duty and thus was rejected.

In summary, the definition of who is to be subjected to the municipal insolvency law should be clear without any ambiguity.

**B. Who can file an application for Municipal
Insolvency and the Jurisdictional Courts?**

United States ("US") has stringent requirements for filing an insolvency application by the municipality. Clause 109(c) of the United States Bankruptcy Code states that the municipality should be bankrupt, specifically authorised by its State law, to file for insolvency and desire to effect a plan to adjust its debts.⁷⁷ Insolvency, as per clause 101(32) of USBC, means that the municipality is either not paying its debt as it becomes due, unless disputed, or unable to pay its debt as it becomes due.⁷⁸

In India too, when a municipality is filing on its own, it should have the authorization of the State. The State is responsible for all related matters like

⁷⁵ Municipal Corporation of Greater Mumbai vs. Abhilash Lal & Ors, (2020) 13 SCC 234.

⁷⁶ The Vizag hospital was resolved under insolvency in July 24. MGM Healthcare submitted a resolution plan of INR 1.71Bn against outstanding creditor claims of INR 13.62Bn.

⁷⁷ United States Bankruptcy Code, 11 USC §109(c) (U.S.A.) [hereinafter 'USBC'].

⁷⁸ *Id.*, §101(32).

earmarking different municipal areas, assignment of taxes, devolution of duties, nominating members to council etc.

However, given the political-economy scenario, it is going to be the rarest of rare occasions when the TMs will seek such permission, and the State will grant the same. This will result in a delay, which will make matters worse for the municipality. Detroit's bankruptcy experience shows that the longer one waits for intervention, the harder it is. *"For 50 years, Detroit's economy, its physical infrastructure, and its social structure had been on a steady decline. And the political system did nothing whatsoever about it."*⁷⁹ England requires local authorities' CFO to issue a section 114 notice whenever the accounts are in imbalance; however, the fact that the incumbent management will be replaced acts as a disincentive for delaying the notice.⁸⁰

Thus, to circumvent the aforesaid agency problem, in addition, financial and operational creditors⁸¹ too should be allowed to file for insolvency of a municipality in case the dues are unpaid for a long, maybe a longer period of outstanding, post overdue date, can be prescribed, (say 120 days – 180 days) as municipalities may have seasonality in their revenue cycle. Moreover, such filings will help municipalities that may have inefficiencies. It is explained later in the paper that these inefficiencies can be reduced by the appointment of a resolution professional/administrator, resulting in both improved financial and operational performance.

⁷⁹ The Pew Charitable Trusts, *After Municipal Bankruptcy – Lessons from Detroit and other local governments*. (2015), <https://www.pewtrusts.org/-/media/assets/2015/08/after-municipal-bankruptcy-pdf.pdf>.

⁸⁰ Eugenio Vaccari & Yselt Marique, *When liquidation is not an option: A global study on the treatment of local public entities in distress* (2022), available at <https://pure.royalholloway.ac.uk/en/publications/when-liquidation-is-not-an-option-a-global-study-on-the-treatment>.

⁸¹ Operational creditors are the ones who provide goods and services to the municipality.

The threshold of default for operational creditors can be further classified into two buckets. A lower amount for medium, small, and micro enterprises (“MSME”), say INR 5 Mn and a higher for others say INR 50 Mn. This is because MSMEs will face stress bereft of adequate working capital.

i. Project-wise Applications should be Encouraged.

One should take a leaf out of the real estate insolvencies and allow project-wise filing where the lenders have lent, or the creditors have supplied goods/services against a particular project. In a similar vein, where a municipal bond issued by the municipality has a charge on a particular project, an insolvency application should be restricted to that project. The application will lie against the municipality only where the borrowing is of a general nature and cannot be ascribed to a single or a group of projects. This will ensure that the working of the full municipality is not disturbed, and at the same time, resolutions can take place in pockets where the distress emanates.

ii. Jurisdictional Courts for Filing of Insolvency Application.

The tribunals for municipal insolvency should be the same as under the IBC. Municipal insolvencies are not likely to be a frequent phenomenon, and thus, having any kind of special tribunals will add to the cost of the exchequer.

C. Control/Oversight of Municipal Affairs

There are two scenarios in which the question of control/ oversight arises when TMs go bankrupt; in the first scenario, the municipality itself is insolvent and in the second, where either a project of the municipality or a public-private partnership performing duties on behalf of the municipalities is insolvent.

i. The Municipality is Insolvent.

Constitutionally, there is no bar to appoint a Resolution Professional/Administrator to look after the affairs of TMs in case the States choose to appoint the person and designate as an “*Administrator.*”

In March 2024, the Brihanmumbai Municipal Corporation (“BMC”) that controls the city of Mumbai completed two years under an administrator rule, the longest it has functioned without elected representatives in its history. Further, the elections are not expected before October 2024 till the time State elections are over. In this period of two years, bereft of elected representatives, the city issued work orders for INR 1,500 Bn,⁸² the liabilities of BMC were at an all-time high of INR 1,900 Bn.⁸³

The aforesaid is not an aberration. In fact, all of Maharashtra’s 27 municipal corporations are being run by State appointed administrators since the tenure of elected representatives expired amidst COVID-19. The combined budget of these 27 municipal corporations is INR 1100 Bn.⁸⁴ Further, Bengaluru Mahanagara Palike has been without an elected body since late 2020; it did not have one between 2006 and 2010. Chennai was without an elected body between 2006 to 2010.⁸⁵

The above incidents clearly depict that an administrator can be appointed by the State to oversee the affairs of the municipality. Thus, an amendment may be carried out to grant insolvency Courts the power to appoint such an Administrator/Resolution Professional, on the advice of the State, of requisite qualification, compulsorily in case debt and default are proven to the Court.

⁸² Pratip Acharya, *Longest period without elected representatives: BMC completes two years under administrator rule*, THE INDIAN EXPRESS (Dec. 30, 2023).

⁸³ Richa Pinto, *Mumbai: Mega Infra projects push up BMC’s liabilities to a record high of I.9L cr*, THE TIMES OF INDIA (Dec. 14, 2023), <https://timesofindia.indiatimes.com/city/mumbai/mumbai-mega-infra-projects-push-up-bmcs-liabilities-to-a-record-high-of-rs-1-9l-cr/articleshow/105971621.cms#:~:text=MUMBAI%3A%20The%20financial%20liabilities%20of,in%20the%20last%20five%20years>.

⁸⁴ *The Tyranny of Back-Door Governance*, MINT (Jan. 30, 2024), <https://www.livemint.com/news/municipal-corporations-and-the-tyranny-of-backdoor-governance-11706531614204.html>.

⁸⁵ *Id.*

Furthermore, the Constitution does not provide an outer limit of time till which date the municipality can function without an elected body, though our endeavour should be to define a timeline for the purpose of insolvency resolution.

A few other jurisdictions, including the United States and Australia, have in their armoury the concept of appointing an Administrator in case of municipal distress. The Indian insolvency regime has developed its own concept of an Administrator for insolvencies of financial institutions wherein the Reserve Bank of India (“RBI”) nominates an Administrator who is endorsed by the Tribunal to act as Resolution Professional. We can model the municipal Administrator on the same lines wherein instead of RBI, the State nominates the person.

In addition, in the insolvency of a financial institution, RBI also appoints a panel of experts to assist the Administrator as these insolvencies are complex. The Constitution already has a provision for the appointment of experts under Article 243R⁸⁶ wherein “*the State may provide for the representation in Municipality of persons having special knowledge of experience in Municipal Administration.*”

Thus, the Administrator, in conjunction with knowledgeable experts, can be roped in to advise on the affairs of the municipality when TMs default. The mandate of the Administrator should be to roll out a plan within a defined period (say one year, extendible by another six months) that will obviate the distress of the municipality. In addition, a five-year plan should be prepared. It should be noted that currently, annual budgets of TMs are prepared without

⁸⁶ INDIA CONST., art. 243R.

a medium-term or long-term time horizon. Thus, forecasts of infrastructure requirements and the associated capital requirements do not exist.⁸⁷

Some of the other immediate steps of the Administrator will be like that of a CIRP: taking control and custody of assets, collating claims, appointing professionals, and forming a CoC. In addition, identify wasteful expenditures that can be slashed and embark on the preparation of a resolution plan. The Administrator, along with experts, can identify sources of distress and alleviate them in multiple ways. A few of the common actions that may be taken are described below; the truly innovative and novel solutions will belong to the realm of experts in a particular situation.

a) Increasing the Number of Public-Private Partnerships

More than a hundred years ago, before Chapter 9 of USBC came into being in the case of *Kaufman v City of Tallahassee*,⁸⁸ the Supreme Court of Florida commented that “*a city's functions have become more and more ministerial, in that its duties consist largely, if not entirely, in the management of public utilities such as waterworks and sewerage systems, electric lighting and power plants, gas plants, telephones, and street railways for the financial advantage and profit of the city. According to the Court, it took very little stretching of this doctrine to say that no municipal function is governmental, a city is not a political subdivision of the State, not a government but purely a business, commercial, proprietary management of local public interests.*” This was a

⁸⁷ Fifteenth Finance Commission, *A Municipal Finance Blueprint for India* (2022), <https://www.janaagraha.org/files/Municipal-Finance-Blueprint-for-India-Janaagraha.pdf>.

⁸⁸ Randal C. Picker & Michael W. McConnell, *When Cities Go Broke: A Conceptual Introduction to Municipal Bankruptcy*; 60 UNIVERSITY OF CHICAGO LAW REVIEW 425 (1993).

revolutionary assertion for the time, though no Courts acted on the aforesaid doctrine.⁸⁹

However, a century later, the assertion that cities have become ministerial does seem to be true. Thus, some of the services provided by TMs may be suitably structured as a business, commercial-oriented PPP, with TMs holding a 26% share. The service providers will have to adhere to strict Service Level Agreements (“SLAs”). In case the existing service providers are from the private sector, better SLAs may be designed or more efficient service providers sought. In fact, some of the areas where the private sector may have better capabilities can be completely outsourced/privatised.

Liberalisation of service delivery, in some but not all areas, will bring the role of markets to the fore, which will not only enhance the level of service but also keep prices in check. As an example, the Delhi discoms were privatised in 2002, 51% being held by private players and 49% by the Delhi Government. The aggregate technical and commercial losses, which were 50% at the time of privatisation, have come down to about 5% today. PPP/privatisation will also help eliminate subsidies and charge a fair price, a task often rendered difficult for politicians in an electoral democracy when TMs are directly providing the service. Moreover, citizens are more amenable to paying a service charge to private players as compared to the Government. The reason all service areas would not be considered under PPP is that some authors⁹⁰ have argued that, in the long run, services suffer if the core capabilities are outsourced.

In addition, PPP’s will shift the financing burden to private players freeing up

⁸⁹ *Id.*

⁹⁰ MARIANA MAZZUCATO & ROSE COLLINGTON, *THE BIG CON* (2023).

municipal resources; the lenders can create a specific charge on such assets as security. Similarly, the administrative overheads too will be reduced on account of a section of activities moving out of municipalities' direct remit.

Furthermore, for the services under PPP, robust audited accounts will be available in accordance with the conditionalities of the finance commissions which can be rolled up into municipalities accounts to the extent of its share.

b) Carve out Areas as Industrial Districts

Though Jamshedpur was not in any distress, the city illustrates how certain areas can be carved out of the municipalities in distress by the Administrators to achieve cost reduction.

In the last week of December 2023, a notification by the Jharkhand government declared that Jamshedpur would be known as Jamshedpur Industrial City. Further, a Jamshedpur Industrial Township Committee (“JITC”) will be formed with up to 27 members of which 11 were to be from Tata Steel.⁹¹

The Constitution, in the proviso to Article 243Q,⁹² states that “*a municipality under this clause may not be constituted in such urban area or part thereof as the Governor may, having regard to the size of the area and the municipal services being provided or proposed to be provided by an industrial establishment in that area and such other factors as he may deem fit, by public notification, specify to be an industrial township.*”

Tata Steel had been providing all the amenities in the township for over a century. However, the requisite legal status evaded them as the Jharkhand

⁹¹ Abhishek Angad, *Confusion over legality of Jamshedpur Industrial City Notification*, THE INDIAN EXPRESS (Dec. 30, 2023), <https://indianexpress.com/article/india/confusion-legality-jamshedpur-industrial-city-notification-9088292/>.

⁹² INDIA CONST., art. 243Q.

Government had not notified the area as an industrial township under the provisions of the Constitution.

Now that the same has been carried out, post receipt of all approvals, State and Centre, Tata Steel will formally take over the township.⁹³ Carving out such areas will reduce the administrative burden and the associated costs for the municipality.

c) Expansion of Municipal Areas for Efficiency

At the other end of the spectrum from carving out is the expansion of municipal areas. A combination of municipalities has both pros and cons. The cons are increased bureaucracy, reduced spirit of competitiveness amongst municipalities and reduced local empowerment.⁹⁴ The pros mostly translate into financial metrics, which are important for a distressed municipality: economies of scale, lower administrative overheads, greater financial and technical ability to solve complex problems, specialisation resulting in lower costs, better debt-raising capacity and better service delivery.⁹⁵

In 2006, ten municipal councils were merged into the Ahmedabad Municipal Corporation (“AMC”) in Gujarat, and in 2020, another was added to the mix. In 2010, three municipalities were merged into the Coimbatore Municipal Corporation. Similarly, in 2021 Pune Metropolitan Region Development Authority and in 2022, the Howrah Municipal Corporation were expanded.⁹⁶ A recent example is the merger of three municipalities of Delhi. Hyderabad,

⁹³ Pavan Burugula, *Tatas may get admin control of Jamshedpur again*, MINT (Dec. 19, 2023), <https://www.livemint.com/companies/news/tatas-may-control-jamshedpur-admin-as-State-gives-nod-11703006726577.html>.

⁹⁴ Ramanath Jha, *Assessing the merger of Delhi’s Municipal Corporations*, 362 OBSERVER RESEARCH FOUNDATION 10 (2023).

⁹⁵ *Id.* at 10.

⁹⁶ *Id.* at 6-7.

too, is planning to merge all municipal corporations and municipalities into the Hyderabad Greater City Corporation.

In case the rural areas are included in the expansion, it may also help enhance revenue due to taxes as well as by higher land value attributed to land in the municipality's possession. This land use change, discussed in a later section, in times of deep distress, can act as a solace to the lenders. In the last decade, many cities, such as Prayagraj, Ahmedabad, Vadodara, Surat, Coimbatore, Chennai, Pune, etc., have merged villages into their municipal boundaries.⁹⁷

Though studies have not been conducted on the effect of such mergers, a 2019 paper infers a positive outcome. It states that "*programs originally meant to generate affordable housing in peripheral areas of the large Indian cities of Mumbai and Chennai have, 20 years later, resulted in thriving communities.*"⁹⁸ A similar exercise of merging municipal areas is in favour in England, too based on independent reports that advocate efficiency and lower costs from merging local entities, as well as by reports commissioned by the Levelling Up, Housing and Communities Committee.⁹⁹

d) Exploring the possibility of expansion in Prime Areas

A variation of the aforementioned expansion theme could be the Administrator requesting the Central Government to release part of the cantonment land to TMs. The request may or may not be granted by the Centre, but an effort can be made. Cantonment land in most cities is now prime land, which can fetch

⁹⁷ *Id.* at 6.

⁹⁸ Anjali Mahendra & Karen Seto, *Upward and Outward Growth: Managing Urban Expansion for More Equitable Cities in the Global South* 37 (Washington, DC: World Resources Institute, 2019), <https://www.wri.org/research/upward-and-outward-growth-managing-urban-expansion-more-equitable-cities-global-south>.

⁹⁹ *supra* note 64, at 166.

handsome revenue. Recently, as a matter of policy, not because of distress, the Central Government released 20,000 acres of cantonment land to State and local bodies.¹⁰⁰ Municipalities can explore joint development with the Ministry of Defence where such a possibility exists without jeopardizing the security needs.

Similarly, several public sector units (“PSUs”) established in the earlier years of independence have extra land in the heart of urban centres. Also, in some cities, single/double railway tracks pass through the city centre. The Administrators and TMs can request the Centre and the ministries in control of PSUs for joint development of such land parcels; the rail tracks can be rerouted.

Such actions will not only result in one-time windfall gains to tide over temporary crises but also will result in a constant stream of property taxes in future.

e) Exploring hitherto unexplored revenue streams in conjunction with savings in recurring costs

Numerous studies, articles and reports have indicated that people at the bottom of the pyramid are the most vulnerable to climate change. The research shows that financial inclusion is one of the best ways to build resilience against the effects of climate change; savings, credit, insurance, money transfers and new digital delivery channels provide a financial buffer as well as aid in recovery and reconstruction.¹⁰¹ However, we are still struggling to find answers *vis-à-*

¹⁰⁰ Harikishan Sharma, *Land portions from 10 cantonment boards to be run by local bodies*, THE INDIAN EXPRESS, (Apr. 8, 2024), <https://indianexpress.com/article/india/land-portions-from-10-cantonment-boards-to-be-run-by-local-bodies-9257140/>.

¹⁰¹ Inclusive Green Finance work stream and Inclusive Green Finance working Group, *Inclusive Green Finance: A Survey of the Policy Landscape* (2020), <https://www.afi-global.org/wp-content/uploads/2020/10/Creative-CV.pdf>.

vis the process to be adopted for inclusion as well as the time period. How to deal with the devastation brought by climate change if it is an annual event in certain seasons?

A mere seven per cent of all climate finance goes toward adaptation purposes. Moreover, much of the effort is focused on “*planned adaptation*”, i.e., building resilient infrastructure.¹⁰² Also, the business cases are harder to make for financing investments in adaptation; they do not yield an immediate return; preventing damage is consumption, which does not generate revenue and is not amenable to easy cost-benefit analysis since resilience is the absence or reduction of climate-induced damage.¹⁰³

To compound matters further, a recent judgment¹⁰⁴ by the Supreme Court expounded on the fundamental rights of citizens. The Court stated that “*the people have a right against the adverse effects of climate change.*” It is difficult to provide this right in a geographic location where destruction due to climate change is a frequent phenomenon.

Municipalities can play a hitherto unexplored role in the aforesaid scenario, which also takes into account the rights of citizens. They can play the role of “*feet-on-street*” for the digital finance providers. Being at the scene, TMs are in a position to judge which adaptation investments will be resilient in the years to come and where they will fail in the next climate calamity. TMs can charge a fee to the digital finance providers for such assessment. Moreover, TMs can explore the possibility of “*planned shifting*” in the expanded areas of

¹⁰² Peter Zetterli, *Climate Adaptation, Resilience, and Financial Inclusion: A New Agenda*, Focus Note, Washington, D.C., CGAP (2023), https://www.cgap.org/sites/default/files/publications/FocusNote_ClimateSynthesis_Final.pdf.

¹⁰³ *Id.*

¹⁰⁴ MK Ranjitsinh & Ors vs Union of India & Ors; Supreme Court of India, Writ Petition (Civil) No. 838 of 2019 with Civil Appeal No. 3570 of 2022 (Supreme Court).

the municipality, described above, where year-on-year havoc is near-certain, and the cost-benefit analysis indicates such an outcome. This would not only curtail periodic expenditure but also be an effort to make another adjacent area a thriving economic hub in a planned manner. In addition, it will be in consonance with the directions of the Supreme Court.

f) Costs of the Insolvency Process

The question of costs will arise on the appointment of the Administrator and the support team. It is a fact that the remit of duties under TMs would require a large team which will be expensive if consultants are employed; Chapter 9 proceedings buttress the fact that proceedings with outside consultants tend to be expensive.

It may not be possible to completely dispense with the consultants. However, in addition other avenues may be explored. One such idea could be to indulge in lateral hiring, which has been tried in a number of government departments across the country. The core team may be hired to work on the municipal payrolls with a market-benchmarked salary for a minimum period of two years. This team can work in conjunction with existing employees.

It would be argued that qualified people will not join for such a short-tenured post as there will be uncertainty post-completion of the assignment. However, this may not be true; all the administrators appointed by RBI for financial sector insolvencies were there for the short term. Moreover, exposure to municipal insolvency will result in an increase in the market value of such individuals as, post the assignment, they will bring to the table a unique set of government institution-related skills. This can be seen from the fact that

boards of private sector banks are full of personnel from RBI, Indian Administrative Services, and public sector banks.¹⁰⁵

ii. **The Public Private Partnership is Insolvent.**

In case a PPP is insolvent the process should be like CIRP with a few modifications. Firstly, in case any portion of the debt of PPP is guaranteed by TMs, an insolvency application cannot be filed without the consent of the municipality. Croatia follows such a practice.¹⁰⁶

Secondly, the rights and obligations of the municipality in PPP, should remain the same post resolution. In case it is decided to liquidate a PPP, either prior consent of the municipality must be obtained or a recommendation for the same by the municipality when the insolvency is initiated; in such instances, any rights of the municipality too would cease. In Croatia, a filing of insolvency against such entities is usually carried out with the consent of the municipality, or local public entity, as called in Croatia.¹⁰⁷

Thirdly, the municipality must get a seat in the Committee of Creditors (“CoC”) to evaluate the resolution plan from a technical perspective. This is because the proposed successful resolution applicant may have been barred or blacklisted earlier by the municipality for poor service or may not be capable of performing the service. However, the resolution professional, CoC and TMs may jointly decide to waive blacklisting or any other deficiency with appropriate guarantees and negotiation.

¹⁰⁵ Gopika Gopakumar, *The silent rise of public sector banker in private bank board*, MINT (Mar. 6, 2024), <https://www.livemint.com/industry/banking/the-silent-rise-of-the-public-sector-banker-in-private-bank-boards-11709725583988.html>.

¹⁰⁶ Lidija Šimunović, *Local public entities in distress – a critical analysis of the Croatian approach, When liquidation is not an option: A global study on the treatment of local public entities in distress* (2022), available at <https://www.royalholloway.ac.uk/media/27056/eugenio-pdf-doc.pdf>.

¹⁰⁷ *Id.* at 143.

D. Committee of Creditors, their Rights, Voting and Deliberations

The rights of creditors will vary in accordance with the two scenarios described above. In case of a specific project or PPP being insolvent, the rights and duties will primarily be in accordance with CIRP alongside the tweaks described above-incorporated, i.e., no variation in rights alongside a seat on CoC for TMs.

However, if the municipality itself is insolvent, novel ideas need to be explored, though certain basics will stay the same as in CIRP: moratorium, priority to interim finance and insolvency costs, cram-down (51% or 66% as the case may be), authorised representative in case of bondholders or debenture holders, similarly situated creditors to be treated equally, etc.

The outcome of a municipal insolvency must be a restructuring, which implies that bereft of a benchmark on market-determined valuation it is difficult to ascertain what is the quantum of distribution the creditors are entitled to. *“The bankruptcy procedures lower the downside risk of borrowing whereas a higher bankruptcy exemption for essential public services could lower the supply of financing. There is thus a trade-off. Where to draw this line is a crucial question in the design of such legislation.”*¹⁰⁸

The conflicting requirements of maintaining essential services and the creditor’s contractual rights imply that the pain of insolvency needs to be shared between lenders and debtors. The insolvency mechanism needs to balance these competing interests.¹⁰⁹

The lesson from the Detroit bankruptcy was similar. All stakeholders – unions,

¹⁰⁸ Liu & Waibel, supra note 48, at 15.

¹⁰⁹ Liu & Waibel, supra note 48, at 19

bondholders, pensioners, city employees, nonprofit foundations, business leaders, State and local lawmakers, and the 690,000 residents accepted cuts; “*Grand Bargain, a collection of settlements that emphasised the policy of cooperation and shared sacrifice.*”¹¹⁰ This is something that all stakeholders in India too should imbibe.

The base document and the plan for an equitable distribution should be prepared by the Administrator and his team. They should prepare a five-year forecast, as anything beyond that is difficult to forecast with the certainty of revenue, expenditure, capital expenditure, and restructuring of operations with a view to identify PPP opportunities and carve out industrial districts. The forecasts should factor in the effects of climate change on infrastructure and financing and iteratively be discussed with the CoC for their input in the periodic meetings. However, the decision of the Administrator would be final and binding.

Implementation of the aforesaid plan will release free cash over the ensuing years that can be paid to both the financial and operational creditors in instalments over an extended period, five to seven years, or as decided by the Administrator in conjunction with the CoC. Unlike a CIRP, where operational creditors are usually paid liquidation value, in municipal insolvency, they should be paid as per the plan. This is because some of the vendors may not be able to provide goods/services for the essential public services in case of a drastic reduction of their receivables, as their working capital limits from banks will reduce on cancellation of their receivables.

Beyond the aforesaid distribution of the free cash, depending on the situation at each municipality some innovative steps need to be carved out to

¹¹⁰ *supra* note 79.

additionally recompense the financial creditors. A few of such possibilities are detailed below.

i. **Refinancing and Restructuring by Sustainability Linked Bonds.**

Refinancing is amongst the first port of call for any professional restructuring of the capital structure. However, in the case of TMs, an added avenue may be tried for reducing the finance cost further, i.e., sustainability linked debt. Many multilateral and financial institutions are willing to provide sustainability linked debt with interest reset on specific performance of an environmental benchmark or on bettering the same. Considering that Indian cities have often grown at the cost of the environment massive opportunities exist to avail such financing. This will save extra cash beyond what would have been achieved by a plain vanilla refinancing.

ii. **Bundling of a Slice of Debt with Privatised or PPP Projects**

The administrator, whilst carving out projects for privatisation or PPP, can assign a portion of the debt, with the consent of the lender, to such projects when the request for quotation for such projects is prepared. This will ensure the servicing of the debt obligation. Also, the potential loss to the financial creditors will be reduced, as from the overall debt exposure, a slice of the debt will be regular.

iii. **Assignment of Land in an Expanded Municipal Territory**

If the financial creditors are institutions and not individual bondholders, and if the geographical location of the municipality permits, it may explore the possibility of including abetting rural areas into itself, acquiring and allocating land in such rural areas to creditors. The land cost post-incorporation into the municipality would increase. This manoeuvre may save the municipality's prime land while at the same time fulfilling the commitment of the creditors.

Moreover, if the financial institution decides to use the land for its own purpose, it will help build infrastructure in another area, decongesting the city. Relevant incentives may be given to such creditors to encourage them to use such land.

Resolving stress by granting land in a resolution plan is not a novel method. It has taken place in CIRP in the case of Jaypee Infratech, wherein 2,594 acres were allotted to financial creditors.¹¹¹

iv. Other Key Points

There should be a definite timeline for approval of the plan, say six months from the date the final draft is prepared. In addition, a representative of the State should also sign off on the plan; not only as a key stakeholder bound by it but also to give added assurance to creditors who are to receive deferred payments.

E. Post Bankruptcy Monitoring

In conjunction with the five-year plan prepared by the Administrator an updated five-year plan needs to be prepared, from the date of resolution, for monitoring the commitments.

Detroit exhibited the importance of post-bankruptcy monitoring. The State of Michigan compelled Detroit to create a financial review commission to oversee the post-bankruptcy plan. The nine-member panel, which includes the Detroit mayor and City Council president, were granted powers to approve contracts and borrowing.¹¹²

Any variation from the plan beyond a specified limit, whether in physical or monetary terms, should require the approval of an independent committee.

¹¹¹ *supra* note 68.

¹¹² *supra* note 79.

The committee should have the Administrator as one of its members, provided, he/she consents for the same.

VII. The Perils of Excessive Leverage for Building Infrastructure

India is on a growth path as China was a few decades ago. The similarities extend to the size of the population and rapid urbanisation. However, there is one crucial difference, the private sector plays a crucial role in India; China is predominantly State-owned enterprises. Nevertheless, the story of China holds important lessons for what not to do whilst allowing municipalities to borrow.

China's tax reforms of 1994, by then-premier Zhu Rongji, centralised taxes, reducing local governments' share of tax revenues, akin to the introduction of GST in India. This is despite the fact that China is the world's most decentralised nation in terms of subnational spending. According to International Monetary Fund research, China's local governments are responsible for 85 per cent of general budgetary spending, bearing significant fiscal duties in areas such as pensions, medical care and unemployment insurance."¹¹³ To fulfil the responsibilities, local governments primarily became dependent on land use rights transactions.

In 2021, local governments earned 40 per cent of their total revenue from the sale of land-use rights. Local governments artificially increased the price of land, which was used as collateral, for credit from banks for infrastructure projects, some of them unviable.¹¹⁴ Chinese officials categorise 14 provinces

¹¹³ Di Lu, *China's local government credit dilemma*, EAST ASIA FORUM (Nov. 3, 2023), <https://eastasiaforum.org/2023/11/03/chinas-local-government-credit-dilemma/#:~:text=The%20depletion%20of%20local%20governments,and%20confidence%20of%20Chinese%20households>.

¹¹⁴ Junhua Zhang, *The bankruptcy of Xiconomics*, GIS REPORTS ONLINE (Oct. 23, 2023), <https://www.gisreportsonline.com/r/china-xiconomics-bankrupt/>.

as being in financial crisis of the thirty-one provinces and municipalities; in some areas salaries of teachers and employees have not been paid.¹¹⁵

Goldman Sachs estimates the debt at USD 23 trillion.¹¹⁶ The International Monetary Fund estimates that the total outstanding off-balance-sheet government debt is around USD 7 trillion to USD 12 trillion, including corporate bonds issued by local-government financing vehicles (“LGFV”), which borrowed money to build roads, bridges and other infrastructure. No one knows what the actual total is, but debt levels have become unsustainable. Domestic banks’ total exposure to LGFV at the end of 2022 was equivalent to USD 6.9 trillion, 13% of the banking sector’s total assets.¹¹⁷

The national goal of high GDP growth and the promotion of officials linked to the achievement of growth targets further exacerbated the problem. This was compounded by the global financial crisis, wherein 70% of the USD 547 billion fiscal stimulus package was raised by the local government.¹¹⁸ Simultaneously, investment returns on many projects fell sharply due to overbuilding. For example, the return on assets in the power and heat supply sector fell from around 4% in 2015 to 1.5% in 2022.¹¹⁹

Economists say \$400 billion to \$800 billion of debt is at high risk of default.¹²⁰ China's government is undertaking a host of measures to obviate the crisis; special bond issuance, debt swaps, loan rollovers, dipping into the

¹¹⁵ *Id.*

¹¹⁶ *Id.*

¹¹⁷ Rebecca Feng & Cao Li, *China’s colossal debt problem is coming to a head*, THE WALL STREET JOURNAL (Dec. 5, 2023), <https://www.wsj.com/world/china/chinas-colossal-hidden-debt-problem-is-coming-to-a-head-83a34dc0>.

¹¹⁸ Lu, *supra* note 113.

¹¹⁹ Nathaniel Taplin, *China’s Teetering Local Debt Mountain*, THE WALL STREET JOURNAL, (Oct. 13, 2023), <https://www.wsj.com/finance/chinas-teetering-local-debt-mountain-in-six-charts-d050700f>.

¹²⁰ Feng & Li, *supra* note 117.

central budget.¹²¹ Local governments are issuing special refinancing bonds to replace some of their off-balance-sheet debt; since October 2023, thirty Chinese provinces and cities have raised the equivalent of around USD 200 billion.¹²² Also, local governments have been ordered to halt problematic PPPs and all the PPPs henceforth will be reviewed by Government authorities in Beijing.¹²³

However, all these measures are just kicking the can down the road. China will have to moderate its growth expectation and the vicious circle of more debt for infrastructure spending to boost GDP. Simultaneously, it should delink the perverse performance incentive linked to GDP growth for its officials.

The lesson for India is that borrowing is needed to build infrastructure but unbridled borrowing for the same will bring misery; a balance is needed from the current .05% of the GDP on one hand to the extreme case of China on the other.

Also, a watch needs to be kept on any creative practices like the artificial land prices of China. BMC's liabilities are an example of the slippery path we are treading. BMC has liabilities of INR 1,900 Bn against a fixed deposit in the bank of INR 870 Bn¹²⁴ and an annual budget of approximately INR 600 Bn, of which INR 280 Bn is revenue expenditure.¹²⁵ BMC claims that the

¹²¹ Kevin Yao & Ziyi Tang, *China orders local governments to cut exposure to public-private projects as debt risk rise*, REUTERS (Nov. 14, 2023), <https://www.reuters.com/markets/asia/china-orders-local-governments-cut-exposure-public-private-projects-debt-risks-2023-11-14/>.

¹²² Feng & Li, *supra* note 117.

¹²³ Yao & Tang, *supra* note 121.

¹²⁴ Pinto, *supra* note 83.

¹²⁵ Mustafa Shaikh, *Mumbai civic body announces annual budget with focus on health and infrastructure*, INDIA TODAY (Feb. 3, 2024), <https://www.indiatoday.in/india/story/mumbai-civic-body-announces-annual-budget-with-focus-on-health-and-infrastructure-2496979>.

liabilities can be clawed back from future revenues as the projects being executed are long-term in nature.¹²⁶ It would be prudent to strictly monitor such an overreach.

Thus, whilst liberalising municipal borrowing, detailed assessments of projects are imperative, or else we will be spending resources on roads and bridges to nowhere and metros and subways connecting ghost cities and colonies. Multiple level checks and balances should be incorporated when municipalities embark on borrowing, both whilst budgeting and when monitoring or auditing.

VIII. Conclusion

The most important function of the municipal insolvency law will be a signalling exercise both for the lenders and municipalities. Clear rules for insolvency are likely to lower borrowing costs through lower interest rates, longer maturity, or both, and thereby increase market access.¹²⁷

The solution for the resolution of insolvency for each municipality will depend on their peculiar circumstances. However, the Administrator will have to balance the tension between the contractual rights of creditors and the need to maintain public services. It is also true that some of the actions described above can be taken whilst TMs are not under stress. However, often, the politico-economic situation makes it difficult to take such actions during normalcy.

India is currently blessed with favourable demographics, where the working population is growing, is expected to peak around 2050¹²⁸ and the cities are

¹²⁶ Pinto, *supra* note 83.

¹²⁷ Liu & Waibel, *supra* note 48, at 17.

¹²⁸ Esha Roy, *India's population growth rate on a steady decline since 90's*, THE INDIAN EXPRESS (Apr. 21, 2023), <https://indianexpress.com/article/india/india-population-growth-rate-8567426/>.

expanding. This gives a golden opportunity to take debt of five-to-twenty-year duration, build infrastructure, repay the debt, and thereafter limit spending to maintenance when the depopulation phase begins.

Delay in creating infrastructure will result in premature decay of TMs, further accentuating the problem of revenue and creating a vicious circle. The timely introduction of municipal bankruptcy law will act as a stimulant for infrastructure economic growth and will let cities blossom.