PRS Capsule April 2019

Key Highlights of PRS

- Finance
  - Supreme Court struck down an RBI circular on stressed assets of banks
  - RBI releases draft enabling framework for Regulatory Sandbox
  - CBDT releases report on profit attribution for taxation of non-residents
  - RBI permits Foreign Portfolio Investors to invest in Municipal Bonds
- Housing and Urban Affairs
  - Draft National Urban Planning Framework
- Fertilisers
  - Cabinet approves extension of the New Urea Policy 2015

Finance

Supreme Court struck down an RBI circular on stressed assets of banks

- RBI issued a circular dated February 12, 2018. The circular laid down a framework for restructuring of stressed assets of over Rs 2,000 crore in a manner such that it mandated the lenders to start the resolution or restructuring process even in case of one-day default by the borrower.
- As per the circular, the resolution plan for such restructuring had to be implemented within 180 days from (1) March 1, 2018 for existing defaults, or (2) the date of first default for any subsequent defaults.
- The Supreme Court, however, struck down the Circular, saying it to be outside the scope of the power given to RBI under Article 35AA of the Banking Regulation (Amendment) Act, 2017.
- The Court reasoned that Section 35AA was proposed by the 2017 Act to authorise the RBI to issues directions only in relation to specific cases of default by specific debtors.

Note: The RBI, in June 2019, has issued a revised circular for resolving stressed assets. The new circular has provision for offering lenders a 30-day period to label an account an NPA.

RBI releases draft enabling framework for 'Regulatory Sandbox'

- In July 2016, the Reserve Bank of India (RBI), created an inter-regulatory Working Group (WG) to study the scope and potential of FinTech (Financial Technology Industry) and review the regulatory framework with which the industry has to comply.
- The inter-regulatory WG was setup under the chairmanship of Executive Director, Department of Banking Regulation (DBR). It also included representatives from RBI, Securities and Exchange Board of India (SEBI), Insurance Regulatory and Development Authority (IRDA), and Pension Fund Regulatory and Development Authority (PFRDA).
- The Working Group's Report gave recommendations to introduce a regulatory sandbox in India.
- Regulatory sandbox is an innovative tool which allows market players to test new financial services or business models with customers in real time and enables regulations that will facilitate delivery of low-cost financial products to customers.
- It ensures an orderly development of fintech, streamline its influence into the financial system, protect the customers and safeguard the interest of all stakeholders.
- The draft framework identified an indicative list of innovative financial products, services and

technologies which could be considered for testing under the sandbox. These products include retail payments, money transfer services, mobile technology applicants, data analytics, financial advisory services, financial inclusion and cyber security products.

CBDT releases report on profit attribution for taxation of non-residents

- The Central Board of Direct Taxes (CBDT) has invited stakeholders' comments on a draft committee report on attribution of profits in case of a permanent establishment (PE).
- The report was prepared by a committee formed to examine the existing scheme of profit attribution to PEs under article 7 of tax treaties concluded by India, as well as recommend changes to Rule 10 of the Income Tax Rules, 1962.
- Currently, taxation of non-residents in India is governed by the provisions of the Income-tax Act, 1961 ("the Act") and the provisions of the Double Taxation Avoidance Agreement(s) [DTAA(s)] concluded or adopted by the Central Government under the powers conferred under Section 90 or 90A of the Act, respectively.
- As per the Income Tax Act, 1961, non-residents are required to pay tax on the income that they receive or accrue from their operations in India. This income is calculated based on the accounts maintained separately for such operations.
- The report recommends the profits derived from India to be defined objectively.

Key observations and recommendations of the Committee include:

- **Discretionary powers:** The Committee observed that the Assessing Officers (a person who has jurisdiction to make an assessment of an taxpayer) have a wide discretion in determination of income of non-residents. It recommended the use of a uniform rule or an objective method for this purpose by the officers.
- **Profit attribution:** It recommended a three factor method using sales, employees, and assets for attribution of profit to an operation, where each factor has an equal weightage. As per committee report, the profits derived from India should be calculated as a certain percentage of revenue, which is the higher of: (i) the global operational profit margin, or (ii) two percent.
- **Users:** The Committee observed that users of an operation should also be taken into account for profit attribution in cases where users contribute significantly to profits, e.g. digital companies. Users can be a substitute to assets or employees, and supplement their role in creating profits.

RBI permits Foreign Portfolio Investors to invest in Municipal Bonds

- The Securities and Exchange Board of India (SEBI) recently notified in a circular that the Foreign Portfolio Investors (FPIs) can invest in Municipal Bonds, subjected to limits set for FPI investment in state development loans.
- The step taken aims to broaden access of non–resident investors to debt instruments in the country. Previously, FPIs were only permitted to purchase securities such as dated government securities, treasury bills and credit enhanced bonds.
- Municipal Bonds are debt instruments issued by a Nagar Panchayat, Municipal Council or Municipal Corporation. The current limit for investment in state development loans is 2% of outstanding stocks of securities.

Housing and Urban Affairs

Draft National Urban Planning Framework

The Ministry of Housing and Urban Affairs recently released the draft National Urban Planning Framework (NUPF), 2018. The NUPF is structured along two lines: (i) 10 core philosophical principles of urban planning, and (ii) these principles are then applied to ten functional areas of urban space and management. Its key recommendations include:

- **City planning:** The draft envisages for a dynamic master plan to be developed with coordination and negotiation between agencies of land use, transportation, infrastructure service provision and economic development for the city planning. A participatory planning approach that embrace diverse resident views, including women, youth and immigrants should be effective in the city planning.

- **Urban finance:** States are required to set norms for cities to meet their revenue expenditure from own revenue and earmark a minimum amount for capital works. In cases, where services can be measured and beneficiaries are identifiable, user charges should be assessed and collected.
- **Urban governance:** Roles and functions of Mayors, Commissioners, and Councils at the municipal level must be fixed. The principle of subsidiarity (a larger and greater body should not exercise functions which can be carried out efficiently by one smaller and lesser) should be used to devolve funds, to ward committees/area sabhas, municipal and regional levels.
- **Transportation:** A Unified Metropolitan Transport Authority, with an overarching transport vision, must be created across all towns. The authority should have power to make decisions on traffic flow planning, which is currently under the control of the traffic police.
- **Housing:** A national housing stock must be created under the National Urban Policy Framework (NUPF) in collaboration with the Ministry of Rural Development, and as per the guidelines of Pradhan Mantri Awas Yojana.

Fertilisers

Cabinet approves extension of the New Urea Policy 2015

- The New Urea Policy-2015 (NUP-2015) which was initially made effective for the period from 1st June, 2015 upto 31st March, 2019, has been further extended by the Cabinet Committee on Economic Affairs.
- The New Urea Policy policy seeks to increase indigenous urea production, promote energy efficiency in production, and reduce the subsidy burden on the central government.