DAILY CURRENT AFFAIRS ANALYSIS

Lakshya Academy®

20 MAY 2024

1 - FIIs to Purchase Sovereign Green Bonds from India:

GS II

Government Policies and Interventions

- **Context:**

- A major step towards funding the country's transition to a low-carbon economy has been taken with the Reserve Bank of India's (RBI) recent decision to permit Foreign Institutional Investors (FIIs) operating within the International Financial Services Centre (IFSC) to invest in India's Sovereign Green Bonds (SGrBs).

- Institutional investors, or FIIs, make investments in assets that are located in nations other than their own.
- The RBI upholds the investment ceilings to control FII involvement, while the Securities and Exchange Board of India (SEBI) oversees FII investments in the nation.

Lakshya Academy ®

- **Sovereign Green Bonds (SGrBs): What are they?**

- The FM declared in the Union Budget 2022–2023 that the government would be issuing Social Guarantee Bonds (SGrBs), a type of loan issued by the government that is intended to finance initiatives aimed at hastening India's shift to a low-carbon economy.
- Through the specific designation of funds obtained through SGrBs for green projects, money utilisation is transparent and accountable.
- Because SGrBs are more in line with sustainable development goals than government securities (G-Secs), they usually have lower interest rates.
- To guarantee the legitimacy of supported projects, SGrBs must be issued in accordance with globally acknowledged green standards and certification procedures.

- The Statutory Liquidity Ratio (SLR), a liquidity rate determined by the RBI for financial institutions, applies to SGrBs.
- Before lending to consumers, financial organisations must maintain SLR with themselves, which limits the amount of money available for other uses.

- The term "greenium" refers to the interest rate differential between SGrBs and G-Secs because SGBs generally yield lower rates than traditional G-Secs.
- To facilitate the shift to a more environmentally friendly future, governments and central banks around the world advise adopting greeniums.

- **Framework for Sovereign Green Bonds:**

- The first SGrB Framework for India was published by the Finance Ministry in 2022, and it described the kinds of projects that will be funded by this bond class.

- **Project Financing:**

- Nine types of green projects will receive funding: clean transportation, renewable energy, energy efficiency, sustainable water management, pollution control, sustainable land use, green buildings, and biodiversity preservation.

- **Projects Not Included:**

- Excluded projects include those that deal with the exploitation of fossil fuels, nuclear power plants, direct waste incineration, gaming, weaponry, alcohol, and palm oil businesses.
- Moreover, landfill projects, hydropower facilities greater than 25 MW, and renewable energy projects utilising biomass from protected regions are not eligible.
- Cicero, a Norwegian validator, evaluated India's framework as a "green medium" with a score of "good governance," indicating agreement with international green criteria specified by the International Capital Market Association (ICMA), a point that the Indian government sought confirmation from to bolster credibility.

Lakshya Academy ®

- distributed via a Uniform Price Auction, a public sale in which a set number of identical goods are offered at the same price.
- Acceptable for Transactions of Repurchase (Repo).
- considered as qualifying investments for SLR.
- acceptable for secondary market dealing.

- **Supervisory:**

- Proceeds from sovereign green bonds will be administered by the Public Debt Management Cell of the Ministry of Finance and put into the Consolidated Fund of India.
- The Comptroller and Auditor General (CAG) of India will oversee the allocation and use of Green Bonds.

- **Benefits:**

- In addition to promoting sustainability objectives, Indian green bonds bolster the value of the rupee by drawing in investors and boosting central bank reserves.
- The price and yield of green bonds may increase due to the limited supply and rising demand for socially conscious investments.

- **What is the impact of FIIs' Green Bond investments on India's Green Transition?**

- As committed at the United Nations Climate Change Conference (COP 26) in Glasgow, 2021, India aims to reduce its carbon intensity by 45% and obtain 50% of its energy from non-fossil fuel sources by 2070. FIIs investing in green projects in India increases the capital pool available to finance these ambitious goals.
- By offering a different source of funding, foreign institutional investors (FIIs) relieve pressure on domestic lenders and free up resources for other purposes.
- The addition of international investors has broadened the pool of possible investors for India's SGrBs, which could result in increased funding for eco-friendly initiatives that support India's Sustainable Development Goals and lessen the country's carbon footprint.
- Through SGrBs, the government hopes to raise Rs 20,000 crore in FY24, and in the first half of FY25, it intends to borrow Rs 12,000 crore.
- Indian green infrastructure projects can benefit from the valuable expertise and experience that foreign investors bring in project management and green technologies.

- **What are the obstacles pertaining to the SGrBs in India?**

- One problem is the lack of a standardised technique or green taxonomy to evaluate an investment's environmental credentials.
- In the absence of precise standards, initiatives run the risk of "greenwashing," in which they make up their environmental friendliness in order to get funding.

Lakshya Academy ®

- **Implementing the Framework:**

- Although India's first SGrB Framework was announced by the Finance Ministry, its enforcement and execution are still crucial.
- Robust monitoring and evaluation systems are necessary to guarantee that funded projects meet the established requirements and promote environmental sustainability.

- **Impact and Selection of Projects:**

- Finding fresh green projects with strong effect and reliable audit trails is essential for the best use of SGrB revenues.
- It may be difficult to secure enough funding for projects with little private resources, such as Distributed Renewable Energy and sustainable energy transition finance for MSMEs.

- **Accessibility of Appropriate Projects:**

- It can be difficult to secure a pipeline of qualified green projects, especially in industries like offshore wind, grid-scale solar power generation, and electric vehicle (EV) production.
- To guarantee a consistent stream of investment possibilities, the government must aggressively promote and reward the creation of such enterprises.

- **The Way Ahead:**

- Increase the viability of green bond issuance and transparency to surmount current obstacles.
- Develop targeted awareness campaigns to highlight the benefits of funding environmentally friendly initiatives.
- By creating a welcoming atmosphere for private investors, you can lower the risks associated with legality, default, liquidity, and other factors.
- Establish strong legal frameworks pertaining to defaulters in order to reassure investors.
- Give top priority to creating a green capital pool in order to boost domestic demand.
- Include environmentally friendly initiatives in the portfolios of institutional investors; this could involve working with organisations in India, such as the Insurance Regulatory and Development Authority of India (IRDAI).

Source → The Hindu

2 - Programme for Green Credit:

GS II

Government Policies and Interventions:

Lakshya Academy®

- **Context:**

- The Ministry of Environment, Forests, and Climate Change (MoEFCC) has made it clear that, in order to qualify for the Green Credit Programme (GCP), ecosystem restoration must take precedence over tree planting.

- **What is the Programme for Green Credit?**

- The Green Credit Programme (GCP) is a cutting-edge, market-based tool created to encourage individuals, communities, businesses, and other stakeholders to adopt voluntary environmental measures in a variety of fields.
- As part of the "LiFE" programme, which was unveiled by the prime minister during the United Nations Climate Change Conference of the Parties (COP26), it is intended to promote environmental protection and a sustainable way of life.

- **Activities Covered: To improve environmental sustainability, the Green Credit programme includes eight main categories of activities:**

- Planting trees to counteract deforestation and boost green cover is known as tree planting.

- Water management: Putting plans into action to effectively manage and preserve water supplies.
- Encouraging environmentally friendly and sustainable farming methods is known as sustainable agriculture.
- Waste Management: Reducing environmental contamination through the use of efficient waste management systems.
- Reducing Air Pollution: Measures taken to enhance air quality and lessen air pollution.
- Maintaining and rehabilitating mangrove ecosystems is essential for maintaining ecological balance.

- **Administration and Governance:**

- The Green Credit Programme is an operational framework that provides a means for people and organisations to make financial contributions towards the restoration of forests that have been classified as "degraded."
- Applications to the Indian Council of Forestry Research and Education (ICFRE), a separate organisation under the Environment Ministry, are made easier in this way.
- The ICFRE is in charge of managing the monetary donations made in support of forest restoration, which is carried out by the corresponding State forest agencies.
- Two years are observed following the afforestation operations, and then the ICFRE evaluates the trees that were planted.
- Following a successful evaluation, every tree is given a value equal to one "green credit." The funding organisation can then use the green credits they have accumulated in two ways:
- First of all, by offering a comparable piece of land for afforestation, they can act as a compliance mechanism for groups required by forest regulations to offset the diversion of forest land for non-forestry activities.
- As an alternative, these credits can be used as a gauge for reporting compliance with corporate social responsibility (CSR) requirements or environmental, social, and governance (ESG) standards.
- Green Credit Acquisition and Calculation: In order to obtain Green Credits, participants must register their environmental efforts on a specific website.
- After a designated agency verifies the actions, the administrator will issue a certificate of Green Credit to the applicant based on the agency's report.
- The determination of Green Credit is contingent upon various elements, including but not limited to resource requirements, scale, scope, size, and other pertinent parameters that are essential to attain the intended environmental results.
- Green Credit Registry and Trading Platform: The creation of a Green Credit Registry, which will assist in tracking and managing earned credits, is a crucial part of the programme.
- The administrator will also build and manage a trading mechanism so that Green Credits can be exchanged on the local market.

- **Importance:**

- India's environmental policies, including the National Environment Policy of 2006 and the Environment Protection Act of 1986, are aligned and offer a framework for enhancing and safeguarding the natural world.
- Together with the GCP, these policies work to protect wildlife, forests, and the environment as a whole.
- In line with India's Climate Goals: The GCP is one element of India's attempts to uphold its obligations under international agreements, including those agreed at COP26.
- It expands the scope of marketable credits beyond CO2 reductions to cover a variety of sustainable measures, complementing the Carbon Credit Trading Scheme established by the Energy Conservation (Amendment) Act, 2022.
- Compliant with Global Ecosystem Restoration Initiatives: The GCP is in line with the United Nations Decade on Ecosystem Restoration (2021–2030), which places a strong emphasis on increasing the scope of restoration initiatives.
- India is taking a holistic approach to this, utilising traditional knowledge and conservation techniques while incorporating all relevant parties in the restoration process.

- **Are Carbon Credits Included in the Green Credit Programme?**

- The Green Credit program operates independently of the carbon credits provided under the Carbon Credit Trading Scheme, 2023, which is governed by the Energy Conservation Act of 2001.
- Carbon credits, also known as carbon offsets, are permits that allow the owner to emit a certain amount of carbon dioxide or other greenhouse gases.
- One credit permits the emission of 1 ton of carbon dioxide or the equivalent in other greenhouse gases.
- An environmental activity generating Green Credits may have climate co-benefits, such as reducing or removing carbon emissions, which can potentially lead to the acquisition of carbon credits in addition to Green Credits.

- **What are the Challenges With the Green Credit Program?**

- Impact on Forest Ecology: Critics have raised concerns that the Green Credit Rules could be detrimental to forest ecology. The rules direct state forest departments to identify 'degraded land parcels' for tree plantation to generate green credits.
- However, this approach has been criticised as unscientific and potentially disastrous for local ecosystems.
- The use of terms like 'degraded' for scrubland and open forests is considered vague and could lead to industrial-scale plantations that may irreversibly alter soil quality, replace local biodiversity, and harm ecosystem services.

- Creation of Green Deserts: There is a fear that the Green Credit Rules might lead to the creation of ‘green deserts’.
- This term refers to areas where tree plantations are established without considering the ecological complexities and biodiversity of the original landscape.
- Such plantations can disrupt the balance of ecosystems and do not support the diverse range of species that a natural forest would.
- The rules have been criticised for measuring forests solely by tree count, which overlooks the multi-layered structure of a functional forest and its associated wildlife.
- Methodological Concerns: The methodology for generating green credits, particularly through tree planting, has been questioned for its environmental soundness.
- Critics are concerned that the methodology does not adequately address potential regulatory gaps and could lead to environmental degradation.
- Pressure on ‘Wastelands’: The emphasis on planting trees on ‘degraded land parcels’ puts pressure on areas often categorized as wastelands, which are ecologically important.
- These areas, like grasslands, play a crucial role in carbon sequestration and supporting unique biodiversity. The push for afforestation in these areas could lead to a loss of endemic species and ecological functions.

- **Way Forward:**

- Biodiversity-Based Afforestation: Shift the focus from tree count to biodiversity-based afforestation, where the goal is to restore diverse native species and ecosystems rather than simply planting a large number of trees.
- This approach ensures that the newly established plantations mimic natural forests and support a wide range of wildlife.
- Technology Integration: Utilise remote sensing and satellite imagery to identify truly degraded lands suitable for tree plantations, minimising the risk of harming existing ecosystems.
- Transparency and Knowledge Sharing: Ensure clear and transparent definitions of terms like "degraded land" and "wasteland" within the program guidelines.
- Promote knowledge sharing and capacity building among stakeholders, including forest departments, businesses, and NGOs, to ensure environmentally responsible practices.

Source → The Hindu

Lakshya Academy ®

3 - Advance Pricing Agreements and Double Taxation Avoidance Agreement:

GS II

Government Policies and Interventions

- **Context:**

- The Central Board of Direct Taxes (CBDT) has achieved a remarkable milestone by signing 125 Advance Pricing Agreements (APAs) during the fiscal year 2023-24.
-
- This surge in APA signings underscores the growing importance of transfer pricing regulations and the efforts to provide certainty to taxpayers.
- In an additional development, India and Mauritius have amended their Double Taxation Avoidance Agreement (DTAA) to curb tax evasion and ensure fair taxation practices.

- **What is an Advance Pricing Agreement?**

Lakshya Academy®

- **About:**

- An APA is a formal arrangement between a taxpayer and a tax authority on transfer prices.
- APAs allow businesses to reduce the risk of their transaction prices being challenged by tax authorities.
- The APA programme has significantly contributed to India's mission of promoting ease of doing business, especially for Multinational Enterprises (MNEs) with a large number of cross-border transactions within their group entities.
- **Types of APAs:**

- **Unilateral APAs:**

- Limit risks for transactions between domestic entities. No guarantee of avoiding double taxation for transactions with foreign entities.
- Relatively shorter proceedings compared to other APA types.

- **Bilateral APAs:**

- Limit risks for transactions between a domestic entity and a foreign entity. Eliminate the risk of double taxation. Longer proceedings as two states must agree.

- **Multilateral arrangements:**

- They mitigate risks for transactions between related entities in 3 or more states, serving as a protective instrument for complex transactions and ensuring safety for both parties, although the proceedings take longer.

- **Key Features of APAs:**

- The APA process is voluntary and will supplement appeal and other Double Taxation Avoidance Agreement (DTAA) mechanisms for resolving transfer pricing disputes.
- The term of APA can be a maximum of 09 years (Including five years prospective and 04 years retrospective if the taxpayer has opted for roll rollback mechanism).
- The procedure ensures the protection of sensitive data provided by businesses.
- Statistical data and summary information are published, but without disclosing names of entities with concluded arrangements or applicants.

- **Importance of APAs for Businesses:**

- Provides tax certainty for determining arm's length price of international transactions.
- Reduces risk of potential double taxation through bilateral or multilateral APAs.
- Reduces compliance costs by eliminating transfer pricing audit risk and resolving disputes.
- Alleviates burden of record keeping by knowing required documentation in advance.
- APAs allow businesses to reduce the risk of their transaction prices being set incorrectly or challenged by tax authorities.
- APAs can be an effective tool for businesses to manage their tax risks and planning.

- **Central Board of Direct Taxes (CBDT):**

- It is a statutory body, established under the Central Board of Revenue Act, 1963, and is a part of the Department of Revenue in the Ministry of Finance.
- CBDT provides essential inputs for policy and planning of direct taxes in India, at the same time it is also responsible for administration of direct tax laws through the Income Tax Department.

- **Double Taxation Avoidance Agreement (DTAA):**

- A DTAA is a tax treaty signed between two or more countries. Its key objective is that tax-payers in these countries can avoid being taxed twice for the same income.
- A DTAA applies in cases where a taxpayer resides in one country and earns income in another.
- DTAAs can either be comprehensive to cover all sources of income or be limited to certain areas such as taxing income from shipping, air transport, inheritance, etc.
- In 1983, India and Mauritius agreed on the DTAA to prevent double taxation. The DTAA applies to residents of both countries.

- **What Does the India and Mauritius DTAA Amendment Entail?**
- **Principal Purpose Test (PPT):**
- The amended protocol introduces the Principal Purpose Test (PPT) to the India-Mauritius Double Taxation Avoidance Agreement (DTAA).
- The PPT denies treaty benefits if obtaining those benefits was the primary purpose of any transaction or arrangement.
- **Article 27B:**
- A new article, Article 27B, is included in the treaty, defining the 'entitlement to benefits.'
- This article specifies conditions under which treaty benefits, such as reduced withholding tax on interest, royalties, and dividends, are denied.
- **Focus on Preventing Treaty Abuse:**
- The amendment aims to address concerns related to tax evasion and avoidance through the abuse of the DTAA.
- By incorporating the PPT, the revised treaty seeks to ensure that tax benefits are not misused for improper purposes.
- **Uncertainty Regarding Past Investments:**
- Despite the amendment, clarity is lacking regarding the treatment of past investments made under the previous provisions of the DTAA.
- The Ministry of Finance is yet to issue clarification regarding the applicability of the new provisions to existing investments.

Source → The Hindu

Lakshya Academy®

4 - Decentralised Industrialisation in Tamil Nadu:

GS II

Government Policies and Interventions

- **Context:**

- Tamil Nadu's economic landscape is undergoing a significant transformation, moving beyond its agricultural roots to embrace a more diversified and industrialised economy.

- This shift is largely attributed to the emergence of cluster capitalists and 'entrepreneurs from below,' who are driving growth in various industry sectors.

- **How Diversified and Industrialised is Tamil Nadu's Economy?**

- Tamil Nadu's farm sector accounts for a lower share (12.6%) of its gross value added (GVA) and employed labour force (28.9%) compared to the national average.
- The state has a higher share of industry, services, and construction in its economy relative to the all-India figures.
- Tamil Nadu's agriculture itself is diversified, with the livestock subsector contributing a significant 45.3% of the farm GVA, the highest among all states.
- The state has developed numerous industry clusters across various sectors like textiles, engineering, leather, food processing, etc.
- Gujarat is more industrialized than TN, with the factory sector generating 43.4% of the state's GVA and engaging 24.6% of its workforce, compared to TN's 22.7% and 17.9% respectively.
- However, Gujarat also has a higher share of agriculture in its GVA (15.9%) and workforce (41.8%) compared to TN's 12.6% and 28.9%.
- This makes Gujarat's economy less diversified and balanced compared to TN.

- **What Factors have Driven Tamil Nadu's Economic Transformation?**

- **Decentralised Industrialisation:**

- Tamil Nadu has only a few major business entities with annual revenues over Rs 15,000 crore.
- However, TN's economic transformation has been driven by medium-scale businesses with turnover ranging from Rs 100 crore to Rs 5,000 crore, with some reaching the Rs 5,000-10,000 crore level.
- The industrialisation has been decentralised and spread out through the development of clusters.

Lakshya Academy®

- This decentralised approach has allowed for a more diverse and balanced economic landscape.

- **Cluster-Based Development:**

- Cluster development is a form of economic development that involves placing businesses in a specific geographic area.
- The goal is to increase productivity and maximise regional efficiency.
- Examples of successful clusters in TN:
- Tirupur: Cotton knitwear (employs 800,000 people);
- Coimbatore: Spinning mills and engineering goods;
- Sivakasi: Safety matches, firecrackers, and printing;
- These clusters have not only created employment opportunities but also fostered a culture of entrepreneurship and innovation, contributing to the overall economic development of the state.

- **Diversification Beyond Agriculture:**

- The creation of employment in cluster towns has reduced Tamil Nadu's workforce dependency on farming, leading to diversification beyond agriculture.
- This shift has expanded the state's economic base by providing alternative employment options.

- **Entrepreneurship from Below:**

Lakshya Academy®

- Entrepreneurs from more ordinary peasant stock and provincial mercantile castes have played a crucial role in driving the state's economic transformation.
- These entrepreneurs have built and expanded businesses in various sectors, contributing to the overall industrialisation and economic development of Tamil Nadu.
- Diverse community involvement, has contributed to the success in achieving industrialisation and diversification beyond agriculture.

- **Social Progress Indices:**

- High social progress indices resulting from public health and education investments have likely contributed to Tamil Nadu's relative success in achieving industrialisation and diversification beyond agriculture.
- The state's focus on social development has created a conducive environment for economic growth and transformation, leading to improved living standards and economic opportunities for its residents.

- **What is the Decentralised Industrialisation Model?**

- **About:**

- Decentralisation involves the systematic distribution of powers and functions across different political and economic agents in society.
- It encompasses both political and economic dimensions, including the decentralisation of decision-making, ownership of means of production, structure of production, and location of production.

- **Key Features:**

- Dispersion of industrial activities across rural and peri-urban areas, reducing dependence on urban centers.
- Promotion of small and cottage industries, owned and controlled by local communities, to foster local entrepreneurship and economic empowerment.
- Emphasis on labour-intensive production methods to generate employment opportunities and alleviate rural poverty.
- The utilisation of local resources and skills to meet local needs and promote sustainable development.
- Interdependence between different village industries creates a self-sustaining economic ecosystem.
- Equalisation of production and distribution through the decentralised location of production units.

- **Benefits:**

- Facilitates balanced regional development and reduces spatial inequalities.
- Promotes inclusive growth by providing economic opportunities to rural communities.
- Enhances resilience to economic shocks by diversifying industrial activities across regions.
- Fosters community participation and ownership in the development process.
- Supports sustainable development by utilizing local resources efficiently and reducing environmental impacts.

- **Challenges:**

- Limited technical capacity can lead to greater inefficiency.
- Decentralised models may lead to increased costs due to a loss of economies of scale, especially in procurement.
- Skilled labour may not be uniformly available across regions in a decentralised model and may result in skill gaps in certain locations.

Lakshya Academy ®

Source → The Hindu

LAKSHYA ACADEMY®