

M. A. Oommen

FISCAL DECENTRALISATION TO LOCAL GOVERNMENTS IN INDIA

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Edited by  
M. A. Oommen

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## CHAPTER FIVE

# THE ROLE OF STATE FINANCE COMMISSIONS IN FISCAL DECENTRALISATION IN INDIA

V. N. ALOK

...As far as funds are concerned, the awards of the State Finance Commissions should be fully honoured. There are reports that State Finance Commissions are not constituted, of them not giving awards in time, and of these awards not honoured when given, all of which erode punchiest raj.

—Excerpts from the Speech of Prime Minister Dr Manmohan Singh on June 29, 2004

### I. Introduction

In most developing countries a trend has been noted in the last two decades towards increasing decentralization of the public sector. The period has witnessed a significant rise in local democracy with growing realization that devolution of political, administrative and fiscal authority to local units of government is one of the best ways to deepen democracy and increase efficiency. It was also felt that responsibilities for expenditure be devolved with concomitant revenue to maintain fiscal accountability (Bird, 1993). Seemingly, this shift along with privatization and deregulation has reduced the authority of national governments over economic policies.

India is also keeping pace with this trend. New systems of local and intergovernmental finance are being established as part of the evolution. The trend has been noted, particularly since early nineties with the passage of 73<sup>rd</sup> and 74<sup>th</sup> Constitutional Amendments that accelerated the process of decentralization with greater devolution and delegation of powers to local governments and the recognition of panchayati raj institutions (PRIs) and

urban local bodies (ULBs) in the book of statute as institutions of self-government.

Consequently, Part IX and IXA have been inserted into the Constitution for PRIs and ULBs respectively and State legislature has been made responsible to transfer functions, listed in the newly created Eleventh Schedule and Twelfth Schedule. The State is also required to transfer the interrelated powers to enable them to carry out the responsibilities conferred upon them. Under the Constitution Amendment Act (CAA), the state legislature is authorized to devolve the specific responsibilities, powers and authorities to the local bodies to enable them to function as 'institutions of self-government'. The legislature of a State may both empower the rural and urban local bodies to levy, collect and appropriate certain taxes, duties, tolls and fees, etc, and also assign to them the revenues of certain state level taxes subject to such conditions as are imposed by the state government. Further, grants-in-aid may also be provided to these local bodies. Resulting from the CAA, the number of PRIs as on April 2005 stood at 248968 of which 236350 are Gram Panchayats, 6097 are Block Panchayats and 543 are Zilla Panchayats (Table1). On the other hand, ULBs by the end of December 2004 numbered 3723 in all States. This number consists of 109 Municipal Corporations, 1432 Municipalities and 2182 Nagar Panchayats, (Table 2).

Fiscal arrangements necessitate every State under Article 243 I and 243Y to constitute, at regular interval of five years, a finance commission (SFC), and assign it the task of reviewing the financial position of local bodies and make recommendations on the sharing and assignment of various taxes, duties, tolls, fees etc and grants-in-aid to be given to the local bodies from the consolidated fund of the State. The conformity Acts of the CAA provide for the composition of the commission, the qualifications for its members and the manner of their selection. Every recommendation of the commission together with an explanatory memorandum is to be laid before the legislature of the state.

It is about one and a half decade since Part IX and IX A were incorporated into the Constitution. During the period, one could have found enough reasons to cheer. Conformity Acts have been enacted in all the States<sup>1</sup>. Elections have been conducted in almost all States<sup>2</sup> barring Arunachal Pradesh, Jharkhand and Puducherry. Women have been elected as Mayor for city governance and *Sarpanch* for rural local

<sup>1</sup> The 73<sup>rd</sup> and 74<sup>th</sup> Constitutional Amendment Acts are the Union Acts to establish the third tier of governments and the conformity Acts are state legislations.

<sup>2</sup> Many States have had a second and third round of elections since the Constitution was amended.

governance. All States except three<sup>3</sup> have constituted their SFC. Most States have received their second-generation SFC recommendations<sup>4</sup>. Notwithstanding, local bodies in almost all States continue to be starved of finances causing major impediment in their growth and effective functioning. The problem is compounded when it is seen with the expanded role and responsibilities of the local bodies after CAA became effective and the 11<sup>th</sup> and 12<sup>th</sup> Schedules were inserted.

Ideally, the functional responsibilities should be closely linked to the financial powers delegated to the local government. In practice, huge mismatch between these two exists leading to a severe fiscal stress at the local level. Own revenues of local bodies are generally adequate to meet only a part of their organisation and maintenance (O&M) requirements. Therefore they are dependent on the higher level of governments to finance their activities. The SFCs are mandated to examine not only the revenue-sharing arrangements between the State governments and the local bodies, both rural and urban, but also the entire range of subjects concerning assignment of taxes, transfers of power and such other aspects for improving the financial health of local bodies. In this case, the CAA does not draw any distinction between the plan and non-plan financial requirements of the local bodies. Therefore SFCs are not confined only to the assessment of non-plan expenditure of the local bodies for recommending the devolution of funds and financial powers to the local bodies at various levels. It is to be noted here that the Union finance commission constituted under Article 280 has been looking only the non-plan expenditure requirements of the States.

Against this backdrop, the paper attempts to review the working of SFCs and their role in fiscal decentralization in India across states. The paper also attempts to identify some of the emerging issues related to the efficacy of SFC in fiscal decentralization. For this, nearly forty SFC reports, both first and second generation, have been analyzed. In many

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<sup>3</sup> The entire States of Meghalaya, Mizoram and Nagaland have been excluded from the operation as per article 243 M(2).

<sup>4</sup> Third Finance Commission has also been constituted in a number of States, *e.g.* Andhra Pradesh, Assam, Bihar, Gujarat, Haryana, Himachal Pradesh, Karnataka, Kerala, Madhya Pradesh, Maharashtra, Punjab and Rajasthan. Some of them, *e.g.* Bihar, Kerala, Maharashtra, Punjab have submitted the report. The State of Bihar constituted the fourth SFC.

cases, actions taken by the respective State Governments on the SFC recommendations have also been considered.<sup>5</sup>

The chapter is in four sections. The first section is introductory. Section II examines issues related to functional and financial devolution in India across states in the wake of seventy third and seventy fourth amendments. Section III, as the title of the chapter indicates, critically examines the reports of the SFCs under various heads. Section IV is by way of summary and conclusion. The scope of the examination is essentially limited by the available information. The overview presented in the chapter is a midterm review that can be outdated in future.

## II. Functional and Financial Devolution\*

India is a federal parliamentary democracy. The PRIs and ULBs are seen as the 'third tier' of government. This has also made India the most representative democracy in the world. Today, about 2.2 million representatives stand elected to the three rungs of PRIs and three levels of ULBs. Of these in PRIs, more than 40 per cent are women and 27 per cent belong to marginalized sections – SCs and STs. At the village panchayat level, on an average each elected person's constituency comprises about 340 people or 70 families (GoI, 2006).

Article 243G of the Constitution empowers PRIs to function as institutions of self-government for the purposes of a) preparing plans for economic development and social justice for their respective areas and b) implementing schemes for economic development and social justice in their respective areas for various subjects including those twenty-nine functions listed in the Eleventh Schedule. Similarly, under Article 243 W, eighteen functions have been enumerated for ULBs. However, both the lists are merely illustrative and indicative. Unlike the division of powers and functions, as spelled out in the Union and State List in the Constitution, no such clear demarcation exists between the State and PRIs/ULBs. It is for the State Legislature to make laws regarding the devolution of powers and functions to the PRIs and ULBs.

Though, almost all states and union territories (UTs) have claimed that they have transferred subjects in varying degrees to the PRIs and ULBs, by enacting laws in conformity with the CAA, functional domain of PRIs

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<sup>5</sup> Oommen (1998); Peterson and Mathur, (2006); and Oommen, (2006) have also analyzed SFC reports of three to five States and Alok (2004) presented the analysis of about twenty SFC reports.

\* This part is drawn from Alok (2006).

and ULBs pertains to only traditional civic functions in several states. Functional domain is without adequate developmental responsibilities in those states where either the intermediate Panchayats or the District Panchayats were absent for decades. States, where they existed for long, have only repeated the provisions of the old statutes in their new laws with marginal adjustments. Moreover, many State Governments have not framed the relevant rules or guidelines as a follow up measure. A few States realized that transfer of additional functions would accompany the concomitant funds and functionaries to local bodies, enabling them to perform the specified responsibilities. At the same time, the local bodies are also not very clear about the role they are expected to play in the new federal set up. The fact of the matter is that almost all the subjects enumerated in the Eleventh and Twelfth Schedules are State-concurrent, involving duplication and overlapping.

Another challenge before the State Government has been the identification of activities to the appropriate tier of the three-tier-PRI system. Traditionally, the lowest level panchayat, *i.e.* the village panchayat (VP) has been the most active in almost all States. Generally, the VPs carry out major functions including core functions whereas intermediate and district panchayats in most States are 'allotted supervisory functions or act mainly as executing agents for the state government' (Jha, 2004:3). In this connection, a Task Force of the Union Ministry of Rural Development on Devolution of Powers and Functions upon PRIs has evolved the activity-mapping model on the principle of subsidiarity that states that any activity which can be undertaken at a lower level must be undertaken at that level in preference to being undertaken at any higher level<sup>6</sup>. Present status on activity mapping can be seen in table 3. In most states, the functions devolved upon the PRIs are in the nature of 'subjects' rather than in terms of 'activities' or 'sub-activities'. Only 'some states like, Andhra Pradesh, Kerala, Gujarat and Madhya Pradesh have broken the 29 subjects into activities and sub-activities' (Oommen, 2004:7). In Kerala, even the complementary legislation has been issued to change the role of key line agencies (World Bank, 2004).

It is a general perception that PRIs and ULBs are financially and technically under-equipped to perform even the core functions, not to speak of the welfare functions and other economic functions related to agriculture and industries (see box 1 and 2). Hence many of the core functions, which traditionally belonged to local bodies like, drinking

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<sup>6</sup> The newly created Union Ministry of Panchayati Raj also provides technical assistance and expertise to State Governments to accomplish activity mapping within the time frame.

water, rural roads, street lighting, sanitation, primary health etc. have not been transferred fully in some states and are being performed by the line departments of the State Government or the parallel parastatals. As a result, the per capita total expenditure of PRIs remains abysmally low in all States except Karnataka, Gujarat, Andhra Pradesh, Maharashtra, Kerala, Chhattisgarh and Rajasthan (see table-4)<sup>7</sup>

### Revenue

Powers to impose taxes by the local bodies was considered imperative to be enshrined in the Constitution under Article 243H and 243X to impart certainty, continuity and strength to the PRIs and ULBs respectively. The Minister, while moving the 73<sup>rd</sup> Amendment Bill in Parliament, argued: "that unless the Panchayats are provided with adequate financial strength, it will be impossible for them to grow in stature" (Oommen, 2004:1). Devolution of taxes to local bodies can easily be linked with the activities assigned to them, which vary from State to State. From the long list of Eleventh and Twelfth Schedules, certain basic functions could be said to be in the exclusive domain of PRIs and ULBs. Even these essential services require huge funds. To this end, the devolution of taxes to the three tiers of the PRIs needs to be linked to the activity mapping for the devolution of functions and functionaries.<sup>8</sup>

Table 5 reveals that a variety of taxes have been devolved at different levels of PRIs. The relative importance of these taxes varies from State to State. The intermediate and district panchayats are endowed with very few taxes whereas village panchayats are given substantial taxing powers. In a number of cases, under the tax rental arrangement, the village panchayat collect taxes and pass on to the higher level of panchayats (Jha, 2004: 4). From the list, property tax, land cess, surcharge on additional stamp duty, tolls, profession tax, advertisement tax, non-motor vehicle tax, octroi, user charges, etc. contribute the maximum to the small kitty of own revenue, which contributes only six to seven percent in the total expenditure of PRIs (table 7). In most States, property tax contributes the maximum revenue. However, this remains an inelastic tax due to inefficient administration in its collection. Its assessment is based on

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<sup>7</sup> However, the data pertaining to local governments in the reports of national finance commissions are not consistent. However, it has to be kept in mind that fiscal data for PRIs, available from any source, is not comparable.

<sup>8</sup> Resolution of the First Round Table of Ministers-in-Charge of Panchayati Raj – Kolkata, July 24-25, 2004, organized by the Ministry of Panchayati Raj, Government of India.

annual rental value of taxation with its associated evil, *i.e.* under-declaration of rentals. However, some progressive States have reformed the tax structure and use unit area method in the determination of the tax base.

After own revenue, the assigned revenue is the closest to local body finances. Such revenues are levied and collected by the State Government and are passed on to local bodies for their use. Some States deduct collection charges. The practice in assigned revenue is also marked by large inter-state variations. However, the typical examples of assigned revenue are: surcharge on stamp duty, cess or additional tax on land revenue, profession tax, entertainment tax, etc. In many states, these taxes form part of the own revenue of local bodies.

### **Borrowings**

No reference is made in the CAA to loans and borrowings by PRIs and ULBs. While ULBs, with the approval of the respective state government, have floated bonds in the market, the PRIs are not empowered to raise loans either from public or private sources (Oommen, 1995: 21), (Jha, 2000: 105) and (Rajaraman, 2003: 25).

### **III. State Finance Commission**

Generally, proceeds from own sources contribute only a small share of the local pool. Local bodies generally rely more on fiscal transfers from State government in the form of shared taxes and grants (table 7). State taxes are shared as per the recommendations of SFC. The SFC created, under article 243-I and Y, is viewed as the sub-national equivalent of the Union finance commission formed under article 280 in the Constitution. The legal provisions for the SFC are, therefore, similar to that of the Union finance commission except the wordings of the first paragraph of article 243-I that provides for the constitution of the SFC 'at the expiry of every fifth year.' This is not akin to the provision exits under article 280 constituting Union finance commission 'at the expiry of every fifth year or earlier'. The missing part 'or earlier' disallows the constitution of a new SFC before the completion of the five-year-period. The article mandates SFC to review the financial position of the PRIs and ULBs and make recommendations to the Governor on the principles that should govern:

1. The distribution between the State and the local bodies of the net proceeds of the taxes, duties, tolls and fees

leviable by the State, and their *inter se* distribution between the PRIs and ULBs at all levels for such proceeds,

2. The determination of the taxes, duties, tolls and fees which may be assigned to, or appropriated by, the PRIs and ULBs;
3. The grants-in-aid to PRIs and ULBs from the consolidated fund of the State;
4. The measures needed to improve the financial position of the PRIs and ULBs
5. Any other matter in the interest of sound finance of the PRIs and ULBs

In practice, with the notable exception of Kerala and Tamil Nadu, most states have faithfully reproduced the constitutional provisions word by word while framing the terms of reference for the SFC. However, these states have not been so faithful to other constitutional provisions stipulating the state to enact a law prescribing the composition of the SFC, qualifications of the members and procedures. This has weakened the autonomy of the SFC. Arguably, the oversight has resulted in many other shortcomings that many experts and commissions have repeatedly pointed out. Some of them are noted below.

### **Delay in the Constitution of SFC**

As pointed out earlier, the constitutional provision leading to the timely constitution of SFC is flawed. Many state governments aggravate it by not constituting it even at the expiry of every fifth year. In some cases, only the chairman and secretary are appointed initially, other members and even terms of reference for the SFC come much later *e.g.* Andhra Pradesh, Assam, Manipur, Punjab and Tripura and the recent two cases are the third SFCs of Maharashtra and Rajasthan. In some cases, SFC has not been constituted. The provision of the Constitution requires the Governor of the state to constitute the 1<sup>st</sup> SFC within one year from the date of the CAA, *i.e.* 24 April 1993. Except Bihar, Goa, Himachal Pradesh, Kerala, Maharashtra, Manipur, Punjab, Rajasthan, Tamil Nadu and Tripura, all other states did not comply with this stipulation. The Government of Sikkim did constitute the first SFC only after three years since the date of the CAA. The postponement in the constitution of SFC, partial constitution, and delay in submission of report obstructs the cycle and its

connection with the Union finance commission. Ideally, at this point of time, the fourth SFC should have been in office in most states.

### **Non-synchronization with Union Finance Commission**

The CAA provides that the Union finance commission should suggest measures to augment consolidated funds of states based on the recommendations of SFCs. However, the last two Union finance commissions, *i.e.* 11<sup>th</sup> and 12<sup>th</sup> were handicapped due to the non-availability and non-synchronization of the SFC reports for the relevant periods. The 11<sup>th</sup> Finance Commission even recommended to delete the words 'on the basis of the recommendations made by the Finance Commission of the State' from sub-clauses (bb) and (c) of article 280 (3) of the Constitution.

### **Qualifications of SFC Members**

SFC like the Union Finance Commission needs expertise in public finance and economics. So far, adequate consideration for knowledge was hardly seen in the constitution of SFCs. The Chairmen of first SFCs were drawn generally from amongst the civil servants, either serving or retired. (*e.g.* first SFC of Andhra Pradesh, Assam, Goa, Harayana, Kerala, Karnataka, Madhya Pradesh, Manipur, Orissa, Punjab, Puducherry, Sikkim, Tamil Nadu, Tripura and Uttar Pradesh). Frequent transfers of the serving civil servants appointed in the SFC lead to frequent reconstitution of the SFC, *e.g.*, Assam, Bihar, Goa, Gujarat, Maharashtra, Orissa, Punjab and Rajasthan. It may be noted that the first SFC of Goa was reconstituted five times and its counterparts in Gujarat and Maharashtra four times. Bihar constituted the first SFC in April 1994 only to be reconstituted later and not to submit its report ever<sup>9</sup>. This erodes the foundation of the technical institution like SFC and adversely affects its approach, continuity and quality.

### **Response by the State Government on SFC Report**

Article 243 I (4) stipulates state government to present before the Legislature of the State every recommendation made by the respective SFC together with an explanatory memorandum as to the action taken

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<sup>9</sup> The second SFC also did not submit its report despite its reconstitution several times. Recently, the fourth SFC of Bihar has been constituted.

thereon. The provision is akin to article 281 related to the action taken by the Union government on the recommendations of Union finance commission. However, the respective government treats this institution and its recommendation very differently. It can be easily observed that key recommendations of the Union finance commission are implemented without modification and other general recommendations are respected and considered at various policy-making exercises. However, at the state level, little attention is paid even to the principal recommendations of the SFC. In several cases, the recommendations are rejected. In many cases, they are accepted through the action taken report, but not implemented by not issuing government orders. In some cases, despite issuance of government orders money is not released. In two cases, -second SFC reports of Karnataka and Maharashtra -the reports have been neither considered nor placed in the State Legislature. The report of second SFC of Kerala was submitted to the legislature without any action taken report three years after it was submitted.

### **Local fiscal data deficiencies**

SFCs get frustrated due to the non-availability of reliable fiscal data on most aspects of state-local finances on which to base analysis and get inferences. These include internal revenue and expenditure data for both PRIs and ULBs, the funds transferred to them from upper levels of governments in the form of devolution and grants, data related to assignments of functions and taxes from the state government. Since an SFC ceases to exist after the submission of its report, many SFCs could not have access to the data generated and scrutinized by the previous SFCs. Most SFCs have indicated these limitations in their reports. In fact, neither the local body, nor state directorate of Panchayats or municipalities, nor local fund audit, or accountant general of the state, or, the Reserve Bank of India, or the central statistical organization, or the ministry of panchayati raj, or ministry of urban development, or the planning commission have consistent fiscal data on local bodies. Many SFCs, have attempted to gather data from the thousands of PRIs and hundreds of ULBs. The first SFC of Andhra Pradesh, Assam, Himachal Pradesh, Karnataka, Madhya Pradesh, Uttrakhand, Uttar Pradesh and second SFC of Andhra Pradesh, Assam, Karnataka, Kerala, Madhya Pradesh, Uttrakhand and Uttar Pradesh are clear cases. However, data presented in these reports cannot be compared with other sources. In some cases, the SFC adopted the technique of sampling. The 11<sup>th</sup> Finance Commission recommended Rs 2000 million for the creation of database

by local bodies. Only Rs 930 million out of this could be utilized, hardly 46 percent. Subsequently, all states have accepted the report of the task force on accrual based accounting format prepared by the Comptroller and Auditor General (C&AG). Some states have implemented the accounting format for PRIs and ULBs.

### **Inconsistent Methodologies of various SFCs**

In order to address the common terms of reference, various SFCs have adopted different methodologies. Many of them attempted to estimate, in their own fashion, the resource gap. The definition of resource gap also varies from one report to another even in the same state. In some cases, unique method is employed to quantify the resource gap. After all these exercised, lump-sum *ad hoc* grants were recommended. Some SFCs have attempted to estimate the gap on a normative basis- though unsuccessfully. The Second SFC of Uttar Pradesh is a case in point.

### **Approaches and Main Recommendations of SFCs – A Review**

Notwithstanding these criticisms, SFCs, in general, have framed their recommendations on the basis of a review of the existing conditions at the state and local level. A cursory glance through forty SFC reports reveals that SFCs have examined some common issues including a) state finances b) state revenue c) state expenditure d) finances of PRIs and ULBs e) fiscal domain of local bodies f) resource requirements g) accounts and audit h) administrative structure i) procedural matters etc. Following these, SFCs have made a number of recommendations. Despite vast inter-state variations in SFC reports, the main recommendations of the SFCs can be grouped under the following four major heads:

1. Global Sharing of revenue between the state and local bodies
2. Assignment of revenues to local bodies;
3. Grants-in-aid to local bodies; and
4. Other measures for strengthening local governance

### **Global Sharing of revenue from the state to local bodies**

The most critical function of the SFCs is the determination of fiscal transfers from the State to local bodies in the form of revenue sharing and grants-in-aid. Since the 80<sup>th</sup> Amendment of the Constitution, following the recommendations of Tenth Finance Commission (1995-2000), a certain percentage of all Union taxes have been devolved to the States. Similarly,

many SFCs have also adopted it for the following reasons: First, the system has a self-policy feature; the local governments automatically share buoyancy of state taxes and levies. Second, there is an inbuilt transparency, objectivity and certainty in this system, as local governments can anticipate, in the beginning of each fiscal year, their share in the divisible pool. Third, this system enables local governments to understand the economy in its entirety. In other words, it induces them for own revenue generation and additional resource mobilization. Fourth, the State Government can be neutral in pursuing tax reforms without considering whether a particular tax is sharable with local governments or not.

This leads to the issue related to the composition of divisible pool. Table 9 reveals wide variations across states in defining the divisible pool and the principle of sharing among the PRIs and ULBs. The first SFC of Andhra Pradesh, Assam and Goa have included the share of Union taxes in the state taxes and non tax revenue to form the divisible pool. However, the first SFCs of Kerala, Madhya Pradesh, and Sikkim and the second SFCs of Orissa and Uttarakhand have not included the share of union taxes and included only the state tax and non-tax revenues. The first generation SFCs of Rajasthan, Tamil Nadu, Uttar Pradesh and West Bengal as well as the second SFC of Kerala have gone a step further and recommended that only the tax revenues of the State form the divisible pool. As an exception, the Karnataka SFCs have adopted a different mechanism by using the phrase "Non loan gross own revenue receipts" in defining the divisible pool. This table illustrates only those States where SFCs have recommended the concept of 'global sharing' for transfer of state revenues.

The SFCs of other States have recommended sharing of only specific taxes or awarded a fixed amount for local governments. The first SFC of Punjab, for instance, has recommended transferring 20 per cent of net proceeds of the five taxes to the local bodies, *i.e.* stamp duty, motor vehicle tax, electricity duty, entertainment tax and entertainment tax on cinematography between the PRIs and urban local bodies. Significant inter-state variations can be seen in the mechanism of revenue sharing as different SFCs made different set of recommendations.

### **Assignment of revenues to local bodies**

As per the practice followed in a number of developed and developing countries, the property tax has been assigned to the ULBs and PRIs in almost all the States and it remains the major source of own tax revenue

for most local bodies. Octroi was another tax that was previously assigned to the ULBs only to abolish in later stage in most States. However, it continues to be levied even now in Orissa, Punjab, Goa<sup>10</sup>, Maharashtra<sup>11</sup> and Imphal (Manipur) and is considered to be the most buoyant source of revenue. In a number of States either a surcharge on sales tax or an entry tax is levied in lieu of octroi. The States of Rajasthan, Uttar Pradesh, Karnataka, and Madhya Pradesh fall in this category. The Profession Tax and the Entertainment Tax stand assigned to the ULBs in Goa, Haryana, Kerala, Madhya Pradesh, Maharashtra and Uttar Pradesh. Most States have also authorized the municipalities to collect market fee, fee for registration of cattle and vehicles. ULBs in a number of States including Goa, Gujarat, Haryana, Himachal Pradesh, Maharashtra and Tamil Nadu also collect education cess.

Water Tax, Lighting Tax, Animal and Vehicle Tax, Trade and Callings Tax, Boat Tax, Toll Tax are the other taxes which have been assigned to the municipalities and panchayats in most States.

Many SFCs have tried to rationalize the local tax structure by suggesting reforms in assessment and administration of taxes besides assigning powers to local bodies. SFC of Kerala, Karnataka, Tamil Nadu and Uttar Pradesh for example, have recommended reform in property taxes and have suggested the 'area based' or 'site valuation' system for assessment of property tax. SFC of Assam, Tripura and Uttar Pradesh recommended even vacant land tax.

### **Grants-in-aid to local bodies**

Grants-in-aid are provided to fill the revenue gap of the local bodies so that they can meet the expenditure on basic functions. These can be (a) conditional or specific grants meant for specific purpose, which can be further classified into matching or incentive grants and non-matching grants (b) general purpose grants or block grants based on some criteria or formula meant for additional resources with no conditions attached. Grants can also be either statutory or non-statutory. Statutory grants are compulsory transfers that may be in lieu of abolition or withdrawal of certain taxes such as octroi.

A review of available SFC reports suggests that SFCs have recommended grants-in-aid on various items including salary (Andhra Pradesh, Maharashtra, Orissa), pension (Andhra Pradesh), roads (Gujarat), maintenance (Andhra Pradesh, Kerala), slum improvement (Maharashtra),

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<sup>10</sup> Levied on hydrocarbons at fuel stations in the State

<sup>11</sup> Only Municipal Corporations levy octroi in Maharashtra.

tourism development (Maharashtra), computerization (Uttarakhand, Uttar Pradesh), non-agriculture land assessment (Gujarat) and agriculture to non-agriculture conversion tax (Gujarat). Many SFCs have suggested *inter se* distribution of the grants recommended by the successive Union finance commission for local bodies.

### Other measures for strengthening local governance

Many SFCs also suggested some changes in the legislative and administrative spheres to strengthen the local government institutions. Some of them require action even on the part of the Union Government. A few of these recommendations are listed below:

- Establishment of a local development fund/incentive fund/common purpose fund.- Almost all SFCs with the notable exception of Andhra Pradesh, Assam, Bihar, Goa, Haryana, Orissa and Uttarakhand.
- Local body should be allowed to levy taxes and service charges on all government properties (including the properties of public sector undertakings of the Union and State Governments, Boards, Corporations). The Constitution should be amended for this purpose. – [*Maharashtra (I), Rajasthan (I), Tamil Nadu (I), Uttar Pradesh (I) & West Bengal(II)*]
- The powers, functions and responsibilities of the State Governments and the local bodies may be bifurcated similar to the division of subjects that exists between the Union and the States in the form of the Union and the State Lists. A third list for District Governments may be inserted in the Constitution. – [*Rajasthan (I)*].
- Appointment of State Finance Commission much before the constitution of Union Finance Commission. – [*Andhra Pradesh (II)*].
- Appointment of Tariff Commission to streamline the existing rates, taxes etc of local bodies – [*Assam & Gujarat (I)*].
- Public Accounts Committee for municipal finance – [*Haryana (I) & Punjab(I)*].
- Finance Commission Cell should function in the Finance Department of the State government even after the expiry of the SFC's term to review the implementation of the recommendations of the SFC – [*Karnataka (I), Kerala( I) & Tamil Nadu(I)*]

- Fund for data base, computerization, software etc.- [Karnataka (II) Maharashtra (I) & Punjab (I)]
- Periodic training for local bodies staff- [Andhra Pradesh (I) & (II), Haryana, Karnataka (I), Punjab(I), Maharashtra (I) Tamil Nadu(I) & Kerala (I)]
- Tax Valuation Committee to listen to the objections of the taxpayer regarding Property Tax assessment – [Punjab(I)]
- Creation of municipal service cadre- [Manipur(I)]
- One common legislation for all local bodies to avoid confusion regarding the regulations and bye-laws – [Karnataka(I), Kerala (I), Maharashtra (I), Punjab(I) & Uttar Pradesh(I)]
- Audit of Municipal Corporation accounts by Accountant General of the State- [Uttar Pradesh(I)]
- Privatization of activities like maintenance of street lights and roads and other core services – [Kerala (I), Punjab (I), Tamil Nadu(I) & Uttar Pradesh(I)]
- Privatization of the maintenance of commercial assets – [Tamil Nadu(I)]
- Public private participation for the improvement of essential services – [Maharashtra (I) & Uttar Pradesh (I)]
- Review of the implementation of recommendations of the State Finance Commissions may be entrusted to a statutory authority – [Andhra Pradesh (I)].

### Union Finance Commission

In order that the SFC does not act as a deterrent to the state legislatures transferring responsibilities and revenue to the local governments, the CAA goes out of the way to provide that the Union Finance Commission should suggest measures augmenting states' consolidated funds in the light of the recommendations of SFCs. So far, three Union Finance Commissions, *i.e.* 10<sup>th</sup>, 11<sup>th</sup> and 12<sup>th</sup> have made their recommendations<sup>12</sup>. All these commissions were severely constrained for the reasons mentioned earlier in the section. Nevertheless, all Commissions recommended *ad hoc* grants to PRIs and ULBs. The Tenth Commission made a provision for the year 1996 to 2000 of Rs<sup>13</sup> 43,810 million at the

<sup>12</sup> The Tenth Finance Commission took cognizance *suo motu* of the newly inserted sub-clauses of Article 280(3) regarding local governments as the CAA became effective before the Commission submitted its report.

<sup>13</sup> Rupees 40 = US \$ 1 in the beginning of September 2007.

rate of Rs 100 per capita for passing on to PRIs and Rs 10000 million for the ULBs to be distributed among the states on the basis of the inter-state ratio of slum population of 1971 census. In the absence of formal disbursement certificates by the State Governments, the Government of India could release only Rs 35,674 million to PRIs. Further, the Eleventh Finance Commission recommended an *ad hoc* annual grant of Rs 1600 crore for PRIs and Rs 400 crore for ULBs based on a formula given in table 10. Certain institution building activities such as maintenance of accounts, creation of database and audit were made the first charge of the fund. Inducement to local bodies as institutions of self-governments was the thrust of the grant. The Government of India accepted the recommendations with a caveat compelling local bodies to raise suitable matching resources.

The grant could not be fully utilized. Many state governments and local bodies have raised this point during their interactions with the Twelfth Finance Commission<sup>14</sup>. The Commission had to emphasize this point in its report *'The central government should not impose any condition other than those prescribed by us, for release or utilization of these grants'* (GoI, 2004e:262). In its recommendations, the Commission attempted to adopt the equalization principle and allocated Rs 200 billion to improve the service delivery by the panchayats in respect of water supply and sanitation. It may be stated here that the grants of the Finance Commission are generally ordained for operation and maintenance and therefore differ from that of the union ministries and the Planning Commission. Through this transfer, the Commission, *inter alia* wanted the PRIs to take over the entire central schemes related to drinking water including *Swajaldhara*, which had been non-operational due to non-availability of funds for operation and maintenance. Similarly, Rs 50 billion was recommended for the ULBs with the condition that fifty percent of the grants should be earmarked for the scheme of solid waste management through public private partnership.

#### IV. Conclusions

While the SFCs have a major role to ensure that the democratic decentralization envisaged under the CAA becomes operational and effective, the State Governments have the responsibility to enhance the credibility and acceptability of the SFCs. It is the State Government that

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<sup>14</sup> This can also be seen in the Memoranda of the State Governments submitted to Twelfth Finance Commission at [www.fincomindia.nic.in](http://www.fincomindia.nic.in)

has to enact a conformity act prescribing the number and qualification of members of the Commission. It is unfortunate that most States have considered the appointment of SFC as one of the instruments through which they can please or appease the group of favourites whether from bureaucracy or from outside. It is interesting to note that the composition of the SFCs, including the chairperson, varied between two to five persons that too varied from full time to part time or the mix of both. The qualification, status and background of the members range from anybody to former Chief Minister (Rajasthan) and former Union Minister of State (Andhra Pradesh and Madhya Pradesh). In many States, SFC report is submitted to the State Government and not to the Governor. In addition, the institution of SFC is further weakened in the absence of firm database on local bodies and norms for service delivery. Diverse views, channels and methods of State-local fiscal transfers make their task even more challenging.

Under such surroundings, most SFCs produced second-rate reports without spelling out the principles on which their recommendations are based. Literature, studies and even theoretical models were mentioned without relating to practice. In other words, the chapter on "conceptual framework" or "issues and approach" is not attuned to other chapters including the chapter on recommendations.

It goes without saying that the endowment of financial powers and authority are to be matched by the functions and responsibilities. Most SFCs barely looked at the functional domain of the local bodies as envisaged in the 11<sup>th</sup> and 12<sup>th</sup> Schedule and hardly considered the potential resource generation of PRIs and ULBs while making recommendations for the devolution of funds from the State government to them.

Given the heavy non-plan developmental tasks the local bodies have to perform, the assigned taxes and non-tax revenue sources are unlikely to be adequate. Moreover, the revenue generating capacities of local bodies, whatever is their level, differ from State to State and even within the State. Some have high revenue potential and some have low. Similarly, cost factor in providing services also differs for various reasons including cost disability factor, *e.g.* area under forest or desert. One cannot deny the fact that vast differences are also found within the State. A classic example is the case of Uttarakhand, a newly carved out State from Uttar Pradesh, which has been declared a special category state due to its special features *e.g.* difficult and hilly terrain. Till recently, the State was a part of Uttar Pradesh, a non special category state. No inter-governmental transfer mechanism had ever realized that part of Uttar Pradesh had characteristics akin to a special category state. Intra-state variations postulate the need for

an equalization transfer mechanism through SFCs that assess the needs of the local bodies as well as their efforts to tap their own revenue potential. This kind of normative assessment by the SFCs should have been to ensure the fulfillment of every citizen's entitlement of basic minimum service or a set of local public goods. Unfortunately, such an issue has either not addressed or attempted amateurishly in most SFC reports.

It is expected from any finance commission, be it a Union or state, to evolve a mechanism so that a fine blend of equity and efficiency objectives can be achieved in fiscal transfers. Only this kind of devolution mechanism can promote autonomy. A system of rewards and punishment has to be developed in the State and the SFCs have to initiate and evolve this mechanism. However, a very few SFCs made its recommendations in that direction.

Most SFCs have recommended a medley of taxes, cesses, or even surcharge on State taxes. Given the fact that collection of taxes at the local level is difficult, such type of efforts lead only to the escalation of administrative cost as each tax requires a tax collection machinery. At times, cost of collection exceeds the actual collection of a particular tax. In order to strengthen the revenue base of the local bodies, SFCs could have recommended measures to tighten tax administration for better compliance of existing taxes, rationalization of taxes and recovery of cost through appropriate user charges.

After the CAA, most States made not much changes in their existing laws related to PRIs and ULBs. Panchayat and municipal laws are fragmented in States. For example, in Maharashtra as many as four municipal laws are governing the ULBs.

Like Union Finance Commission, SFC's recommendations are recommendatory not mandatory in nature, but unlike Union Finance Commission, SFC's recommendations are occasionally honoured and often being given cold shoulders. In fact, many states are making a mockery of the constitutional provision. On the one hand, they constitute a body with people of smattering knowledge; on the other hand, they do not even consider the report. If the report is considered, very few recommendations are accepted. In the process, the crucial ones are rejected without assigning reasons. In the action taken report, only numbers are mentioned. In this number game, sometime the most crucial recommendations are found rejected surreptitiously. At the top of it, many times, the accepted recommendations are not implemented. Sometime, money was not released even though actions on these recommendations were notified. The story becomes more funny given the fact that a state Government took three years to only consider the report of the SFC.

Since State Governments do not consider the recommendations of the SFC in time, the major problem regarding the synchronization of the periods of SFC with that of the Union Finance Commission arise. The Eleventh Finance Commission, though, had the reports of the first generation SFCs of most States but these were of different periods of time and except for two (Goa and Orissa), related to only the first or at best the second year of the period covered by the EFC. For this very reason the Eleventh Finance Commission even recommended to delete the words "on the basis of the recommendations made by the Finance Commission of the State" appearing in sub-clauses (bb) and (c) of Article 280 (3) of the Constitution. The Twelfth Finance Commission also faced similar problems.

Considering the poor own revenue base of the local bodies so far, and its high dependency on higher level of governments, the recommendations of State Finance Commission have to be of utmost importance to the local bodies. Since all available SFC reports differ with reference to their approaches and methodologies and even the time period covered by them. Some SFCs have access to data some have not. In such circumstances, it is extremely difficult, if not impossible, to standardize these recommendations. Since, firm data on panchayat and municipal finance are still not available from any source; it is extremely difficult to analyze the impact of SFC recommendations on the finances of local bodies. It is clear, from the progress report of the last fifteen years that though the stipulation of SFC is an innovative and significant feature of the CAA, it lacks teeth and substance.

**Table 1: Number of Rural Governments in Each State/UT as on 1 April 2005**

Sl. No	Name of State/UT	Panchayats by tier				Average Rural Population Per Village Panchayat
		Village <sup>1</sup>	Intermediate <sup>2</sup>	District <sup>3</sup>	Total	
1	Andhra Pradesh	21913	1095	22	23030	2663
2	Arunachal Pradesh	1747	150	15	1912	527
3	Assam	2489	203	20	2712	9911
4	Bihar	8471	531	38	9040	9654
5	Chattisgarh	9139	146	16	9301	1959
6	Goa	190	0	2	192	3537
7	Gujarat	13819	225	25	14069	2447
8	Haryana	6034	114	19	6167	2687
9	Himachal Pradesh	3037	75	12	3124	1915
10	Jharkhand	3746	211	22	3979	2256
11	Jammu & Kashmir	2683	0	0	2683	8593
12	Karnataka	5659	175	27	5861	6456
13	Kerala	991	152	14	1157	24714
14	Madhya Pradesh	22029	313	45	22387	2167
15	Maharashtra	28553	349	33	28935	2067
16	Manipur	166	0	4	170	10284
17	Meghalaya*	5629	0	3	5632	366
18	Mizoram*	737	0	3	740	654
19	Nagaland*	1286	0	0	1286	1556
20	Orissa	6234	314	30	6578	5289
21	Punjab	12445	140	17	12602	1356
22	Rajasthan	9189	237	32	9458	5187
23	Sikkim	159	0	4	163	3357
24	Tamil Nadu	12618	385	29	13032	2711
25	Tripura	537	23	4	564	5198
26	Uttar Pradesh	52028	813	71	52912	2757
27	Uttarakhand	7227	95	13	7335	924
28	West Bengal	3360	333	18	3711	18290

Union Territory						
29	A&N Islands	67	7	1	75	3807
30	Chandigarh	17	1	1	19	6172
31	Dadra & Nagar Haveli	11	0	1	12	17355
32	Daman & Diu	10	0	1	11	12848
33	NCT of Delhi #	0	0	0	0	NA
34	Lakshadweep	10	0	1	11	3939
35	Puducherry	98	10	0	108	3477
	All India	242328	6097	543	248968	3278

Source: Alok (2006)

Note: \* Figures from Report of the Eleventh Finance Commission for Traditional Village/District Councils that exist in these States, however, figure for Nagaland is from the Report of Twelfth Finance Commission

# PRI is yet to be revived.

1. In almost all States it is known as Gram Panchayat.

2. The nomenclature of intermediate rung differs from one State to another. It is known as Mandal Parishad in AP, Anchal Samiti in ArP, Anchalic Panchayat in Assam, Janpad Panchayat in Chhattisgarh & MP, Taluka Panchayat in Gujarat, Taluk Panchayat in Karnataka, Panchayat Union in TN, Kshetra Panchayat in UP and Uttarakhand and Panchayat Samiti in many States, i.e Bihar, Haryana, Himachal Pradesh, Jharkhand, Maharashtra, Orissa, Punjab and Rajasthan.

3. It is also known as Zilla Panchayat/Parishad in many States.

**Table 2: Number of Urban Local Bodies by State as on December 2004**

SL. No.	State	Municipal Corporations	Municipal Councils	Nagar Panchyat	Total	Urban Population (in crore)	
1	Andhra Pradesh	7	109	1	117	2.08	
2	Arunachal Pradesh	ULBs do not exist.					
3	Assam	1	28	54	83	0.34	
4	Bihar	5	37	117	159	0.87	
5	Chattisgarh	10	28	71	109	0.42	
6	Goa	Na	13	Na	13	0.07	
7	Gujarat	7	142	Na	149	1.89	
8	Haryana	1	21	46	68	0.61	
9	Himachal Pradesh	1	20	28	49	0.06	
10	Jammu and Kashmir	2	6	61	69	0.25	
11	Jharkhand	1	20	22	43	0.60	
12	Karnataka	6	41	175	222	1.80	
13	Kerala	5	53	Na	58	0.83	
14	Madhya Pradesh	14	86	236	336	1.60	
15	Maharashtra	16	228	Na	244	4.11	
16	Manipur	9	9	19	28	0.06	
17	Meghalaya	Na	6	Na	6	0.05	
18	Mizoram	Na	ULBs do not exist			0.04	
19	Nagaland	Na	Na	9	9	0.03	
20	Orissa	2	33	68	103	0.55	
21	Punjab	4	98	32	134	0.83	
22	Rajasthan	3	11	169	183	1.32	
23	Sikkim	ULBs do not exist.					
24	Tamil Nadu	6	102	611	719	2.75	
25	Tripura	Na	1	12	13	0.05	
26	Uttar Pradesh	11	195	417	623	3.45	
27	Uttarakhand	1	31	31	63	0.22	
28	West Bengal	6	114	3	123	2.24	
<b>Total</b>		<b>109</b>	<b>1432</b>	<b>2182</b>	<b>3723</b>	<b>28.61</b>	

Source: Alok (2007), Notes: Na means not applicable

As per the CAA there are three types of ULBs. These are (a) Nagar panchayat in areas which are in transition from rural to urban. In many States, nomenclature is different and terms like 'Notified Area Committees', 'Municipal Committees', 'Town Area Committees', 'Urban Station Committees', 'Notified Area Committees' are used. (b) Municipal Councils in smaller urban settlements; it is also called 'Nagar Palika Parishad' and 'Municipality' in some States (c) Municipal Corporations in larger urban areas. In some States, it is called as 'Nagar Nigam', 'City Corporation' and 'Nagar Palikhe'. It is the discretion of the State Governments to identify and define the term of "transitional", "smaller" and "larger" urban areas.

**Box 1****Classification of Functions Listed In Eleventh Schedule****Core Functions**

- Drinking Water.
- Roads, culverts, bridges, ferries, waterways and other means of communication.
- Rural electrification, including distribution of electricity.
- Health and sanitation, including hospitals, primary health centres and dispensaries.
- Maintenance of community assets.

**Welfare Functions**

- Rural housing.
- Non-conventional energy sources
- Poverty alleviation programme.
- Education, including primary and secondary schools.
- Technical training and vocational education.
- Adult and non-formal education.
- Libraries.
- Cultural activities.
- Family welfare.
- Women and child development.
- Social welfare, including welfare of the handicapped and mentally retarded.
- Welfare of the weaker sections, and in particular, of the Scheduled Caste and the Scheduled Tribes
- Public distribution system.

**Agriculture and Allied**

- Agriculture, including agricultural extension
- Land improvement, implementation of land reforms, land consolidation and soil conservation.
- Minor irrigation, water management and watershed development.
- Animal husbandry, dairying and poultry.
- Fisheries.
- Social forestry and farm forestry.
- Minor forest produce.
- Fuel and fodder.
- Markets and fairs.

**Industries**

- Small scale industries, including food processing industries.
- Khadi, village and cottage industries

Note: The Eleventh Finance Commission has given the above classifications to the functions enumerated in the 11<sup>th</sup> Schedule

## Box 2

### Classification of Functions Listed In Twelfth Schedule

#### Core functions

- Roads and Bridges
- Water supply for domestic, industrial and commercial purpose
- Public health, sanitation, conservancy and solid waste management
- Burial and cremation grounds and electric crematoria
- Public amenities including street lighting, parking lots, bus stops and public conveniences

#### Welfare functions

- Safeguarding the interests of weaker sections of society, including the handicapped.
- Slum improvement and up gradation
- Urban poverty alleviation
- Provision of urban amenities and facilities such as parks gardens, playgrounds
- Promotion of cultural, educational and aesthetic aspects
- Cattle pounds; prevention of cruelty to animals

#### Development functions

- Urban planning including town planning
- Regulation of land-use and construction of buildings
- Planning for economic and social development
- Fire services
- Urban forestry, protection of the environment and promotion of ecological aspects
- Vital statistics including registration of births and deaths.
- Regulation of slaughter houses and tanneries.

Note: The Eleventh Finance Commission has given the above classifications to the functions enumerated in the 12<sup>th</sup> Schedule

**Table 3: Current progress on Activity Mapping**

State	Number of Subjects-		Comments
	transferred through legislation	undertook for activity mapping	Activity mapping -
Andhra Pradesh	17	9	Not been completed
Assam	29	29	Not been completed
Bihar	25	0	Consultation process on
Chhattisgarh	29	7	For seven subjects completed
Goa	6	18	Not been completed
Gujarat	15	14	For five subjects completed.
Haryana	NA	NA	Draft prepared.
Himachal Pradesh	26	NA	Consultation process on
Karnataka	29	29	For 26 subjects completed and funds devolved.
Kerala	26	26	For 26 subjects completed and funds devolved.
Maharashtra	18	NA	Not been completed
Madhya Pradesh	23	7	Not been completed
Manipur	22	22	For 22 subjects completed
Orissa	25	7	Not been completed
Punjab	7	NA	Not been completed
Rajasthan	29	18	Not been completed
Uttar Pradesh.	12	NA	Not been completed
Uttarakhand	14	14	For nine subjects completed executive orders issued for three.
West Bengal	29	NA	completed

Source: Government of India (2006), Annual Report 2005-06, Ministry of Panchayati Raj

Note: 'NA' figure not available in the given source.

**Table 4: Per capita Expenditure in PRIs(All tiers)**

No.	State	1990-91	Per capita (Rs)		Annual Growth of Total Expenditure 1998-2003 (%)
			2000-01	2002-03	
1	Andhra Pradesh	205.7	792.9	898.4	11.9
2	Assam	1.1	3.2	3.2	2.2
3	Bihar	18.2	4	37.7	17.3
4	Chhattisgarh	NA	360.8	353.6	11.3
5	Goa	30.1	198.2	418.9	31
6	Gujarat	399.4	1293.5	782.7	-1.6
7	Haryana	54.7	142.1	241.1	26.7
8	Himachal Pradesh	8.6	41.2	59.2	12.7
9	Jammu & Kashmir	0.0	750	851.2	9.6
10	Karnataka	402.6	1296.2	1147.2	5.9
11	Kerala	46.1	644.9	742.5	0.5
12	Madhya Pradesh	44.5	113.9	103.5	2
13	Maharashtra	298.4	685.8	821.2	11.1
14	Manipur	7.0	25.5	37	21.9
15	Meghalaya	81.6	51.6	25.5	4.4
16	Orissa	65.0	37	56.8	25.4
17	Punjab	70.0	85	108.3	9.7
18	Rajasthan	218.9	361.6	382.3	5.7
19	Sikkim	0.0	78.6	74.2	17.7
20	Tamil Nadu	59.7	164.7	152.8	7.6
21	Tripura	5.3	186.1	252.9	5.2
22	Uttar Pradesh	40.9	46.9	43.3	5.1
23	Uttarakhand	NA	49.3	45.9	-2.1
24	West Bengal	24.5	107.0	29.7	5.5
<b>All (24 States)</b>		<b>148.0</b>	<b>324.0</b>	<b>327.8</b>	<b>6.9</b>

Source: same as in table 1.

Note: In the absence of consistent data for the relevant years the growth rate of Bihar, Kerala, Orissa and Uttarakhand pertains to shorter duration than indicated.

**Table 5: Revenue Power of Rural Governments in States at Each Tier**

Tax/Fees	Andhra Pradesh	Assam	Bihar	Gujarat	Haryana	Himachal Pradesh	Karnataka	Kerala	Madhya Pradesh	Maharashtra	Orissa	Punjab	Rajasthan	Tamil Nadu	Uttar Pradesh	West Bengal
House/ Property Tax	V	V	V	V	V	V	V	V	V	V		V	V	V		V
Surcharge on House/Property Tax								V		D						
Tax on Agriculture land for specific purpose	V															
Cess on Land Revenue/ Surcharge	V, I	I		V		V		V	V						V	
Surcharge on Additional Stamp Duty	V	V			I	V	V		I	D				V		V
Tax on professions, Trades, Calling, etc.		V/I	V,D	D		V	V		V	V		V			D	
Octroi				V						V			V			
Entertainment Tax		V	D	V			V	V	I			V			V	V
Pilgrim Tax / fees		V		V			V			V			V			

Tax/Fees	Andhra Pradesh	Assam	Bihar	Gujarat	Haryana	Himachal Pradesh	Karnataka	Kerala	Madhya Pradesh	Maharashtra	Orissa	Punjab	Rajasthan	Tamil Nadu	Uttar Pradesh	West Bengal
Tax on Advertisements	V						V	V								
Education Cess				I								I	I			
Tolls	V	I,D	I,D	V										V	D	V,D
Tax on Sale of firewood and Slaughter Houses		V									V					
Tax on goods sold in a market, <i>Haat</i> , Fair etc.			I,D		I	V					V					
Tax on Shops and Services		V			V	V										
Vehicle Tax	V	V		V			V		V	V	V		V		V	
Animal Tax				V					V	V	V				V	
Conservancy Rate	V	V	V	V				V	V		V	V			V	V

Tax/Fees	Andhra Pradesh	Assam	Bihar	Gujarat	Haryana	Himachal Pradesh	Karnataka	Kerala	Madhya Pradesh	Maharashtra	Orissa	Punjab	Rajasthan	Tamil Nadu	Uttar Pradesh	West Bengal
Lighting Rate	V	V, D	V, I, D	V		V		V	V	V	V	V	I		V, I, D	V, I, D
Water Rate	V	V, D	V, I, D	V	V, I	V	V	V		V, I, D	V	V, I	V, D		V, I, D	V, I, D
Drainage Rate	V			V				V			V				V	V
Spl. Tax for Community Civic Services/ Works					V	V		V	V			V	V, I			
Surcharge on any tax imposed by VP	I			I, D									I			I

Source: same as in table 1

Note: V denotes Village Panchayat, similarly I and D denote Intermediate and District Panchayat respectively. More than one sign indicates the concurrent power of PRIs for the respective tax.

**Table 6: Own Revenue of PRIs (All tiers) (Rs million)**

No.	State	1990-91	2000-01	2002-03	Annual Growth (%) 1998-2003
1	Andhra Pradesh	627.0	1516.5	1708.5	7.6
2	Assam	30.1	73.2	76.1	2.0
3	Bihar	NA	77.1	66.7	4.2
4	Chhattisgarh	NA	573.9	578.7	2.0
5	Goa	10.5	76.5	80.1	2.2
6	Gujarat	274.5	759.2	698.6	-3.1
7	Haryana	293.9	701.4	783.6	9.3
8	Himachal Pradesh	0.2	33.5	53.9	30.2
9	Karnataka	173.3	668.3	594.6	2.0
10	Kerala	313.2	2196.6	2260.1	3.9
11	Madhya Pradesh	119.4	1420.9	1748.1	8.3
12	Maharashtra	342.1	3279.8	4700.7	18.1
13	Orissa	59.0	90.6	55.1	-9.6
14	Punjab	215.6	806.7	987.7	5.7
15	Rajasthan	242.8	368.9	376.8	3.6
16	Tamil Nadu	157.2	572.0	654.4	5.2
17	Tripura	0.1	4.9	6.0	6.8
18	Uttar Pradesh	227.5	588.3	631.7	7.5
19	Uttarakhand	NA	48.7	61.0	4.9
20	West Bengal	142.3	325.3	312.7	2.8
<b>All (20 States)</b>		<b>3251.2</b>	<b>14182.4</b>	<b>16435.1</b>	<b>8.0</b>

Source: same as in table 1

Note: NA – Data not available in the given source.

**Table 7: Per capita Own Revenue of PRIs (All tiers)**

No.	State	Per capita (Rs)		
		1990-91	2000-01	2002-03
1	Andhra Pradesh	12.9	27.4	30.0
2	Assam	1.5	3.2	3.2
3	Bihar	NA	1.0	0.9
4	Chhattisgarh	NA	34.5	33.5
5	Goa	15.2	113.1	118.8
6	Gujarat	10.1	23.9	21.3
7	Haryana	23.7	46.7	50.2
8	Himachal Pradesh	0.0	6.1	9.5
9	Karnataka	5.6	19.2	16.7
10	Kerala	14.6	93.2	94.1
11	Madhya Pradesh	2.3	32.0	38.0
12	Maharashtra	7.1	58.8	81.9
13	Orissa	2.2	2.9	1.7
14	Punjab	15.1	50.1	59.9
15	Rajasthan	7.2	8.5	8.3
16	Tamil Nadu	4.3	16.4	18.9
17	Tripura	0.1	1.8	2.2
18	Uttar Pradesh	2.1	4.5	4.6
19	Uttarakhand	NA	7.7	9.4
20	West Bengal	2.9	5.6	5.2
<b>All (20 States)</b>		<b>5.3</b>	<b>20.1</b>	<b>22.6</b>

Source: same as in table 1

**Table 8: Share of Own Revenue in Total Expenditure of PRIs (All Tiers)**

Revenue	1990-91	2000-01	2001-02	2002-03
Own Revenue (%)	4.5	5.9	6.0	6.8
Others* (%)	87.9	90.7	87.9	92.1

Source: same as in table 1

Note: \* Others include devolution and grants.

**Table 9: Significance of PRIs' Own Revenue**

Year	Share of Own Revenue (%)			Own Revenue of PRIs (Rs million)
	Union Government	State Governments	Panchayati Raj Institutions	
1990-91	63.42	33.21	0.36	3251
1995-96	61.03	35.14	0.31	5680
1998-99	59.65	37.01	0.48	11610
1999-00	60.63	36.30	0.47	13345
2000-01	59.87	37.05	0.45	14182
2001-02	57.61	39.26	0.44	14328
2002-03	59.11	38.43	0.45	16435

Source: same as in table 1

Note: Percentages are worked out by adjusting the own revenue of local governments in the total tax revenue (All India).

**Table 10: SFC Recommendations for Share in State Resources**

State	%	Share of PRIs and Urban Bodies	Basis of distribution
<b>Total Revenue of State:</b>			
Andhra Pradesh(I)	39.24	70%and 30%	Development criteria Population Population, geographical area, performance.
Assam(I)	2.0	Not mentioned	
Goa (I)	36.0	75% and 25%	
<b>Own Revenue of State:</b>			
Andhra Pradesh(II)*	10.39*	65%and35%	Development criteria Not mentioned
J & K (I)	13.5	67% and 33%	
Kerala (I)	1.0	not mentioned	Population
Madhya Pradesh (I)	11.579	25.13% and 74.87%	Population, area, tax efforts ULBs do not exist in the state
Sikkim (I)	1.0	100% and 0%	Population and Distance from Rail Head
Uttarakhand	11.0	42.23 and 57.77	Population (80%); area (20%)
Uttar Pradesh(I)	10.0	30% and 70%	Population and area
Uttar Pradesh(II)	12.5	40% and 60%	
<b>Non-loan gross own revenue:</b>			
Karnataka(I)	36.0	85% and 15%	For panchayats-population, area, index of decentralization and for ULBs population 67% and illiteracy rate 33% [Kar II has followed it]
Karnataka(II)	40.0	80% and 20%	
<b>State Own Taxes</b>			
Kerala (II)	5.5	78.5% and 21.5%	Population
Rajasthan(I)	2.18	77.3% and 22.7%	Population
Rajasthan(II)	2.25	76.6% and 23.4%	Population
Tamil Nadu(I)\$	8.0	60% and 40%	Population
Tamil Nadu(II)	8.0	58% and 42%	Population

West Bengal(I)	16.0	Breakup as per population. district wise	Population and % of SC/ST, non literates
West Bengal(II)	16.0	Breakup as per population. district wise	Population 50% and 7% to other variables, population density, SC/ST, non-literates, IMR, rural population, per capita income.

Source: same as in table 1

Notes: \$ In Tamil Nadu, the divisible pool called pool B consists of sales tax, motor vehicle tax, state excise revenue and other state taxes. The other pool A consists of levies which rightly belong to local bodies i.e. surcharge on stamp duties, local cess and local cess surcharge and entertainment tax. The entire proceeds of pool a taxes are recommended to be distributed to the local bodies.

1\* Second SFC of Andhra Pradesh recommended 10.39% share as additional devolution over and above the existing annual devolution.

**Table 11: Criteria adopted by Union Finance Commissions for *inter se* distribution of grants to States for local bodies**

Criteria	Weight assigned by	
	11 <sup>th</sup> Finance Commission	12 <sup>th</sup> Finance Commission
Population	40	40
Area	10	10
Distance	20	20
Decentralization Index	20	Not Adopted
Revenue Efforts	10	20
Deprivation Index	Not Adopted	10

Source: Report of the Eleventh Finance Commission for 2000-2005 and Report of the Twelfth Finance Commission for 2005-2010

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