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Dr. Amaresh Bagchi was a Member of the Commission from 04.07.2007 to 20.02.2008, the date he unfortunately passed away. The Commission expresses its deep gratitude to late Dr. Bagchi for his signal contribution during his tenure as a Member.

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A Review of Indian Fiscal Federalism

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A Review of Indian Fiscal Federalism

M. Govinda Rao

I. Introduction

Fiscal federalism in independent India evolved over the last 60 years, has held the country together, provided identity and scope for various religious, ethnic, linguistic groups to function and has provided a reasonably flexible institutional framework for the functioning of the multilevel fiscal system. At the same time, it would be erroneous to conclude that the system has worked to the satisfaction of all the groups and surely, there are several areas requiring improvements. There have been appreciable achievements and glaring shortcomings and it is important to identify them with a view to embark on the reforms in policies and institutions. At the same time, market based development in a globalising environment poses significant challenges of creating a competitive environment for which the fiscal system will have to play a lead role and fragmented nature of the polity does not make the task of re-engineering the system any easier. Therefore, the time is opportune for making a detailed evaluation of the functioning of fiscal federalism in India to identify the strengths and shortcomings and initiate the measures needed to re-engineer the multilevel fiscal system and institutions to face emerging challenges. Accelerating growth in the country and making it inclusive calls for a close re-look at the existing multilevel fiscal system.

A notable achievement of Indian fiscal federalism has been to keep the country unified for almost sixty years since the commencement of the Constitution. Despite complex challenges posed by diverse political, economic, linguistic, social and ethnic diversities, the country has remained a unified and vibrant multilevel polity. It has, over the years, achieved considerable success in resolving a variety of conflicts and accommodated dissensions arising from its size and diversity. The Constitution has provided a flexible and yet, a resilient framework for a society characterised as “unity in diversity” and has adjusted to meet the needs, problems and challenges of a changing society. The multilevel fiscal arrangement has provided the institutional framework for the development of the country.

A number of factors have helped in evolving India as a democratic, multicultural, multi-linguistic, multi-religious and multiracial federal polity. The Constitution has provided enough space and scope for every group by ensuring fundamental rights and instituting elaborate checks and balances to safeguard the interests of diverse groups. It has
subordinated the role of the military to the civilian executive and decentralised the power structure to minimise the possibility of military takeover. Over time, with regular and periodic elections, the democratic values have taken deeper roots\(^1\). Independent judiciary has been a great strength in safeguarding the interests of not only various minority groups but also those of the States whenever there were attempts to subvert the Constitutional provisions and apply it in arbitrary and unjustified manner. The Supreme Court’s decision the dismissal of the elected State Governments under Article 356 of the Constitution is justiciable in the case of *S. R. Bommai versus Union of India* is a case in point. It was declared that the Governor of the State can not dismiss an elected State government merely on the ground that the ruling party in the State has lost majority support, but will have to test the same in the floor of the house. The free press in the country too has been a major factor in providing checks and balances and inculcating democratic values. It must also necessary to acknowledge the important role played by the all India services in the initial years of independence in shaping the Indian federal polity. Their competence, independence and objectivity has been often mentioned as a factor that has helped to unify the country though, these values have tended to weaken over time.

In spite of the achievements noted above, there is considerable dissatisfaction with the system of governance and economic management by the Centre as well as sub-national governments. There is a feeling among the experts that the system has entailed significant costs and the constraint posed by it has not helped to reap potential developmental dividends. Furthermore, the fiscal federalism in the country evolved in the context of public sector dominated import substituting plan strategy will have be reengineered to meet the needs of a liberalised economy in a globalising environment. The centripetal bias inherent in the Constitution combined with the adoption of centralised planning in a mixed economy framework, to a considerable extent, has undermined the advantages of a decentralised fiscal system and has hindered the creation of a common market. The assumed gain from fiscal federalism – of efficient provision of public services according to varying preferences of the people in different jurisdictions, is yet to be realised in a satisfactory manner. While the decentralised units were expected to impart dynamism to the economy, they have often indulged in the exploitation of fiscal commons and adoption of protectionist and

\(^1\) In 1976, Mrs. Indira Gandhi invoked Article 352 to declare emergency powers to take over the powers after the Allahabad High Court set aside her election to the Parliament. However, she and the Congress Party were defeated with overwhelming majority when she declared elections in 1977.
populist policies to pass the financing burden of their pet schemes to the non-residents and preferences to locals in employment and business and creation of tariff zones within the country overtly or covertly. Regional disparities in both material progress and human development have shown a steady increase both within and between the States and reducing those remains a major challenge. Despite several amendments to the Constitution to empower the rural and urban local governments, they remain disempowered and the objective of providing efficient levels of public services has continued to be elusive. The country has ceased to be a customs union, as impediments to trade between the regions continue to deny the benefits of a large common market. On the political front, the regional aspirations and search for identities by different groups continues to raise its head from time to time in terms of a demand for separate statehood as seen in the case of Telengana in Andhra Pradesh, Gorkhaland in West Bengal and Vidarbha in Maharashtra. There are many contentious issues – both inter-State and Centre-State that remain unresolved and there are no satisfactory mechanisms or institutions to negotiate and bargain and systems to deal with externalities and settle disputes and foster co-operation. The institutional shortcoming is manifest in many areas, the most important of being the inter-State river water disputes which have become perennial.

There have been several attempts in the past to review the working of the federal fiscal system India and some have made far reaching recommendations. Besides, the detailed studies by various scholars and reports of the Twelve Finance Commissions, various aspects of Centre-State relations were analysed by the Administration Reforms Commission (India, 1969), the Committee on Centre-State Relationship appointed by the Government of Tamil Nadu chaired by Rajamannar (1971) and the Commission on Centre-State Relationships chaired by Justice R. S. Sarkaria (India, 1988). The Sarkaria Commission actually made 247 recommendations in its voluminous report containing 19 chapters covering the entire gamut of issues covering the Centre-State relations.

In spite of these attempts, a fresh review of Centre-State fiscal relationships is opportune for a variety of reasons. First, the general criticism of the Sarkaria Commission’s report is that, by and large, the Commission favoured status quo in the arrangements and the recommendations were meant to effect minimal changes in the system and institutions. This implies that a more detailed review of the economic issues arising from the multilevel governance system is in order. More importantly, the multilevel fiscal system evolved in

2 There are a number of reviews of Indian fiscal federalism presenting the successes and failures. To name a few, Rao and Chelliah (1996), Bagchi (2000), Rao and Sen, 1996 and Rao and Singh (2005).
the context of public sector dominated, heavy industry based, import-substituting industrialization strategy needs to be reoriented to meet the challenges of market based development in a globalising environment. Furthermore, the polity has undergone significant changes and conducting inter-governmental relations in the years immediately after independence when the single party – the Indian National Congress, dominated both Central and State governments is different from a situation when there is a coalition government at the Centre. The emergence of coalition governments at the Centre with regional parties as pivotal members of the coalition with different, often opposing political parties ruling in the States has created frictions in the working of the federation. The need to have effective institutions to negotiate and bargain, rule based systems for conducting intergovernmental negotiations and resolve inter-State and Centre-State matters has not been felt so important and urgent ever before.

The country as diverse in linguistic, cultural, ethnic, religious and economic as India is has multiple loyalties – some that can be mapped by geographical boundaries and others cannot be. Diversity in preferences and multiple loyalties presents several challenges in providing efficient levels of public services and resolving a variety of conflicts both within and between the States apart from those between the Centre and States. Conflict resolution in a diverse society and more importantly creating an accommodating multi-level governance framework calls for re-examination of the Constitutional provisions relating to Union-State relationships. This is essential from the viewpoint of fostering cooperative federalism – a governance framework in which facilitates political harmony and cooperation among different levels of government to accelerate economic growth and reduce poverty. Therefore, the time is opportune to make a detailed review to evaluate whether the institutional framework is strong enough, and solutions offered by the constitutional mechanism are able to satisfactorily deal with the problems of a pluralistic society.

This paper makes an attempt at reviewing the functioning of Indian fiscal federalism in terms of fulfilling the broad objectives of ensuring a stable and secure macroeconomic environment, providing satisfactory standards of social and physical infrastructure and services, ensuring nation-wide market for commodities and factors of production and promoting efficiency in resource allocation and promoting and regulating markets to accelerate growth and creating conditions for a proper state of distribution of income and wealth in the society. The purpose of the review is to highlight the successes, understand its failures and identify areas requiring reforms in both policies and institutions to enable the Indian fiscal federalism to meet the emerging challenges from diversity, globalizing economic environment, information revolution and technological changes.
Theories of Fiscal Federalism: A Review

(a) Traditional Theories of Fiscal Federalism

Fiscal federalism is considered to be an optimal institutional framework for the provision of public services. As observed by Alexis de Toqueville more than a century ago, “The federal system was created with the intention of combining the different advantages which result from the magnitude and littleness of nations” (1980, Vol. 1, p. 163). The basic issue, however, is that of aligning responsibilities and appropriate fiscal instruments to carry them out to different levels (Oates, 1999). The advantages from the magnitude and littleness can be realised only when the functions of different levels of governments and various units within each of the levels are clearly specified so that economies of scale in the provision of services reaped, advantage of a large common market is realised while retaining the individual identities and public services according to the diversified preferences of people across the nation are provided. This involves mapping the public services to various governments and jurisdictions within each level of government depending on their comparative advantage in terms of their capacity and willingness (incentive) to respond to diverse preferences, reap scale economies, and minimize transaction costs in the provision of public services.

An important implementable rule of fiscal decentralization is the clear assignment of instruments to raise revenues to effectively implement the functional responsibilities (Bahl, 2002). Finances should follow functions and the subnational governments should have the capacity to vary the public services as demanded by taxing their residents. Assignment of revenue sources is necessary for, a strong link between the decision to spend and the decision of raise revenues to finance the spending imparts greater efficiency and accountability in the provision of public services. Thus, proper assignment of functions and sources of finance, consequences arising from their overlap and the mechanism to match their functions and finances both vertically among different levels of government and horizontally among different governmental units constitutes the subject matter of fiscal federalism.
From this perspective, fiscal federalism is simply an efficient organisation of the multilevel public sector. As Stated by Oates, “...the term federalism for the economist is not to be understood in a narrow constitutional sense. In economic terms all governmental systems are more or less federal: even in a formally unitary system” (Italics in the original; Oates, 1977; p. 4). Similarly, Bird (2000, p. 135) states, “…in the traditional world of fiscal federalism in principle everything – boundaries, assignments of finances and functions, the level and nature of transfers and so forth – is malleable.”

The above formulation, however, blurs the difference between decentralisation and federalism. According to Watts (1996), the structure can take the form of “Decentralised Unions” which are basically unitary states in which subnational units have greater or lesser degree of policy autonomy devolved to them by the Central Government or formal federations which combine a strong Central Government with sub-central tiers having their own powers. Indeed, there can be considerable divergence between formal and operational federation, but nevertheless, as a rule there is considerable devolution of powers in formal federations.

Thus, formal federal systems, besides decentralisation, have additional pre-requisites. Most importantly, the issue is not merely one of having an efficient assignment system; it is also important to see how the assignments are made and are the assignments extinguishable. Although it is difficult to get instances of classical federalism conceptualized by Wheare (1964) in which, the participating governments are “coordinate and independent”, the assignment system must be determined independently and should have a measure of permanence. There should be an effective system of checks and balances to ensure a measure of permanence. In confederal systems, the assignments are done by lower level governments (States) whereas in decentralized systems, powers are assigned by senior level governments. A federal system is the one in which the entire set of powers – legislative, fiscal and regulatory - are divided in the Constitution or conventions between different levels of government. There is a measure of permanency in the assignments and in particular, the powers given to lower level governments cannot be extinguished by higher level governments (Breton, 2000). Thus,

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1 Not surprisingly as Breton (1981, p. 253) States, “Political scientists who know better, have in their more generous moments treated economists as poor souls with a model in hand in need of an application”

4 Bird (2000) makes a distinction between fiscal federalism and federal finance. In his formulation, under fiscal federalism everything - boundaries, assignments, and the transfers - is malleable, under federal finance these must be taken to be fixed at some earlier (constitutional) stage and not open to further change under normal circumstances.
checks and balances to safeguard the system is an inherent part of the federal system whereas, decentralisation does not necessarily entail that. In other words, all federal systems are decentralized whereas all decentralized systems are not federal. The Constitution and other institutions set up to ensure checks and balances and safeguard the domains of different levels of government are inherent components of a federal system.

The political theories make out the case for federalism on the basis of freedom and representation\(^5\), safeguarding group identities and ensuring security and stability through bargains. On the other hand, economic theories of federalism focus on creating multilevel public sector governance systems to improve efficiency. The traditional analysis or what has come to be known as the first generation theories of economic federalism (Qian and Weinghast, 1997; Oates, 2005) implicitly assume that governments are “benevolent” and as “custodians of public interest”, they seek to maximize social welfare. They demonstrate the superiority of the decentralized system over the centralized provision of public services. The new approaches to fiscal federalism or the second generation theories consider the assumption of benevolent governments unrealistic and take that agents within the governments (bureaucrats and politicians) have their own objective functions operating within the constellation of incentives and constraints depending on the given fiscal and political institutions (Oates, 2008). They model the inter-governmental behaviour in terms of principal-agent relationship, underline the importance of hard budget constraints and focus on the importance of competition – both vertically between different levels of government and horizontally among different units within the same level to enhance efficiency in the delivery of public services.

The normative framework of fiscal federalism laid out by the traditional theory presents the assignment of functions to different levels of government as well as appropriate fiscal instruments to carry them out. Broadly, the theory states that redistributive and stabilization functions belong to the realm of the Central Government due to the innate constraints in carrying them out by sub-national governments. In the case of the former, the constraints are posed by the potential mobility of economic units and in the case of the latter, lower potency of the policy instruments due to spillovers arising from the open nature of sub-national economies. However, in carrying out the allocation function,

\(^{5}\) For a review of various political theories of federalism, see Rao and Singh (2005).
subnational governments have a predominant role. The theory also lays down the norms for the assignment of fiscal instruments to finance the assigned functions. From the efficiency point of view, the decentralised governments should not only refrain from levying non-benefit taxes on mobile economic units but they should actually levy benefit taxation when these mobile units receive benefits from the services provided by them. In addition, there is clearly a case for levying taxes on immobile factors.

A general contention is that decentralised system of governance enables greater efficiency in service delivery. One of the earliest formulations of efficiency rationale for decentralisation was by Tiebout (1956). When there are a large number of localities with different public service – tax mix, and people have footloose mobility, they “vote on their feet” to move to the localities that provide the fiscal package best matching their preferences. In the limiting case, this process can generate an efficient equilibrium outcome. Even when the assumption of ‘footloose’ mobility is relaxed, Oates (1969) shows the superiority of decentralised solution as fiscal differentials are capitalized into property values.

Much of the focus of the first generation theories of fiscal federalism, however, is in demonstrating the superiority of decentralised system over the centralised by exercising their preferences through “voice” – the voters influencing the decisions through the ballot and this is characterized by the ‘decentralization theorem’. The theorem States, “…… in the absence of cost savings from the centralized provision of a (local public) good and of inter-jurisdictional externalities, the level of welfare will always be at least as high (and typically higher) if Pareto-efficient levels of consumption are provided in each jurisdiction than any single, uniform level of consumption is maintained across all jurisdictions” (italics added; Oates, 1972, p. 54). Notably, in this formulation, the lower efficiency is due to uniform provision of public services and not due to centralization per se. Nevertheless, ability of the centralized system in meeting diverse preferences is limited by informational and political constraints and hence, the superiority of decentralized provision of public services (Oates, 1999).

The decentralisation theorem rests on two basic assumptions. First, the governments are benevolent and maximize outputs of public goods so as to maximize the welfare of their residents. Second, centralised provision necessarily results in uniform level of public outputs in all jurisdictions. The support for this is taken from the fact that it is difficult for

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6 This, in fact could result in loss of efficiency on another count. Levying benefit taxes on mobile manufacturing activity could result in source-based as against residence-based taxation. See Oates (1999).
the Central Government to obtain the information needed to provide public services according to diverse tastes and preferences. Second, it may be politically infeasible for the Central Government to vary the levels of public services across jurisdictions. These are discussed briefly below.

The classification of public sector according to Musgrave-Oates trilogy – of redistribution, stabilization and allocation results in the first two being predominantly carried out by the Centre and the last – the allocation function being mainly the responsibility of subnational governments. The considerable information asymmetry in carrying out the allocation function at the Centre places the decentralised governments at an advantage. In real world situations, however, it is impossible to attribute divide the powers to the levels of government corresponding to Musgrave-Oates trilogy. Even conceptually, efficiency of the decentralised system in the allocation function presumes that there is an omniscient Central Government or a Central planner who has perfect information about the preferences of people, degree of spillovers and magnitude of scale economies of different public services in order to be able to determine the assignment system and a system of transfers. In a setting of perfect information, it would be possible for the benevolent central planner to provide different sets local public services that maximizes the social welfare. As Breton (1995, p. 185) has noted, “If Central Governments could perform the difficult task of estimating marginal spillover flows and designing the appropriate grants program, a division of functions is not only unnecessary but wasteful.” However, informational and political constraints could prevent the Central planner from generating an optimal pattern of local public services (Oates, 1999).

The issue is important because, potential welfare gains from decentralisation are large. The gains depend on variations in demand and the gains are inversely related to the price elasticity of demand for local services. Although there are no empirical studies on the demand for local services in India, the evidence from the US shows the price elasticity of demand for local public services is low (Bradford and Oates, 1974; Rubinfeld, 1987). Indeed, technological developments could lower the information cost and reduce information asymmetry and this may favour increased centralization in respect of some services. It is also possible that often the case that is made for decentralization is, in fact, a case for privatization rather than decentralisation. Thus, the assignment system requires to be reviewed from time to time (Tanzi, 2002).

Footnote: Interesting Breton (1965) was the earliest to demonstrate the superiority of decentralization which was later developed by Olson (1967) and Oates (1968) into what has come to be called the “decentralization theorem”.
An extension of the traditional theory is the assumption that solutions to fiscal federalism must be found in “co-operative federalism”. Implicit in this proposition is that the assignment system should be unambiguous and powers given to sub-national governments can not be extinguished so that the latter can exercise unfettered choice in their assigned domains. As argued by Coase (1960), clear assignment works like the assignment of property rights. Efficient provision of public services in their respective domains and internalizing externalities and spillovers requires bargaining between different governmental units. Clarity in assignments reduces transaction costs and enables “Coasian bargains” in which, the jurisdictions bargain with one another for mutual gains and resolve many issues arising from spillover of costs and benefits among them. This is the essence of ‘co-operative federalism’ (Inman and Rubinfeld, 1997a, 1997b). However, co-operative federalism is possible only in cases where there is motivation to enter into bargains for mutual gains, there is a measure of equality in the bargaining strength and there is an effective referee and monitor to ensure efficient bargaining processes.

(b) Political Economy Approaches to Fiscal Federalism

This branch of literature on fiscal federalism draws heavily from the developments in public choice and industrial organization (information) theories – It does not assume an altruistic government and motivation of public officials as common good in the Samuelson–Musgrave tradition. Instead, it assumes that participants in the political processes have their own objective functions and seek to maximize their own gain rather than the welfare of the society (Oates, 2005). In other words, the new literature recognizes the importance of motivations of incentives of the bureaucrats and politicians. According to the traditional theories, welfare gains accrue from more efficient provision of public services due to better matching of preferences. Thus, the trade off is between the efficiency gains from meeting diversified preferences and inability to internalize the spillovers at the subnational level. The models employing the public choice approach (the second generation theories or SGT), in contrast, bring out the trade off in terms of better “accountability” of decentralized levels versus better coordination of policies to internalize spillovers (Seabright, 1996). Thus, despite significant differences in the models employed under the public choice approach, many of them produce a trade off between centralization and decentralization which is fundamentally similar. As stated by Besley and Coate (2003, p. 2628), “…the lay insight remains that heterogeneity and spillovers are correctly at the heart of the debate about the gains from centralization”.

Report of the Commission on Centre-State Relations
There are three distinct sets of theories under the new approach to fiscal federalism or the second generation theories. The first is the application of developments in industrial organization theory to fiscal federalism, particularly modeling the multilevel fiscal arrangements in terms of the principal-agent framework. The second strand focuses on the problems arising from the soft budget constraints and derives motivation from the fiscal crisis precipitated by exploitation of “fiscal commons” leading to perverse behaviour of subnational governments, particularly in Latin America. Finally, the third strand employs more formal political economy approaches based on legislative structure and electoral process to analyse different kinds of fiscal outcomes under centralised and decentralized politics. Among others, this strand examines the outcomes from “yardstick competition” under the rubric of “competitive federalism”.

(i) Fiscal federalism in the principal-agent framework:

The application of industrial organization theory to fiscal federalism is mainly to model the behavior of agents in terms of principal-agent problem. There are two approaches adopted in such models. In the first the Central Government is treated as the principal and the States are treated as agents (Levaggi, 2002). In this formulation which is akin to what Inman calls “Administrative federalism”. In this model, States are treated simply as agencies that respond to the directives of the Centre. In the second formulation, electorate is taken as the principal and elected officials are taken as agents. In one such formulation Tommasi (2003), demonstrates that decentralisation is preferable even in cases of perfect homogeneity of preferences. In this, the case for decentralisation depends not only on differences in tastes, but also on the potential for better local control or accountability. Similarly, Seabright (1996) considers elections as “incomplete contracts” in his analysis and concludes that while centralization allows for greater coordination of fiscal decisions, decentralization promotes preference matching and greater accountability. Thus, like in the case of traditional theories of fiscal federalism, heterogeneity and spillovers are the critical factors determining gains from decentralisation (Besley and Coate, 2003). Thus, the basic trade off is between gains from coordination and providing public services according to preferences and ensuring greater accountability in the public service provision under decentralisation.

(ii) Fiscal federalism and soft budget constraints:

The second strand of literature in the new approaches to fiscal federalism deals with the problems arising from the exploitation of “fiscal commons” by subnational
governments and in particular, the problem of soft budget constraints. Prud’homme, argues that decentralised levels of government have strong incentives to ‘raid the fiscal commons’ to create destabilising impact on the economy. The perverse incentives and poor efficiency arising from them is brought out by applying the concept of “soft budget constraint” advanced by Kornai (1979, 1980) which was originally used to explain the behaviour of public enterprises in socialist economies, to analyse the behaviour of decentralised governments. The perverse incentive arises from the existence of soft budget constraints as the authorities in decentralised governments expect the higher level governments to bail them out of their fiscal problems of continuing deficits and increasing stock of debt. The approach adopts a sequential game-theoretic framework to explain the way in which perverse expectations are formed. In the first stage, Central Government declares that it will not bail out fiscally distressed decentralised governments. Of course, the latter do not take this as credible because bankruptcy of a local government can have serious consequences and this can spill over to other jurisdictions. Therefore, in stage two, the subnational governments may continue to profligate and build up deficits and debt. Faced with this fiscal debacle at the subnational level, in stage three, the Centre will have to take a call on whether or not to bail out the decentralised government.

The literature identifies various political and economic factors that undermine fiscal discipline at subnational levels and identifies various sources of soft budget constraints. Rodden, Eskelund, and Liteck (2003) analyse the experiences of various countries and identify five important sources of soft budget constraints for subnational governments which are (i) ill defined responsibilities to units and functionaries; (ii) federal transfers, (iii) borrowing by subnational governments and bail outs by higher level of government; (iv) absence of a strong system of private markets (land, capital), (v) history and precedents.

An important application of the soft budget constraint is the concept of Market Preserving Federalism (MPF) which according to Weingast (1993, 1995) is the ideal type of federalism. He puts forth five preconditions for the MPF which are: (i) existence of a hierarchy of governments clear delineation of function to each level; (ii) subnational autonomy to provide public services and to regulate in areas assigned to them; (iii) the national government should have policies to ensure a common market to allow for factor and product mobility; (iv) all governments, particularly the subnational governments face hard budget constraints; and (v) the
political authority of different governments are institutionalized so that one level or a governmental unit can not abridge, expand or extinguish the powers of the others.

The ideal type of federalism is the MPF in which the above five conditions are satisfied the most. Effective intergovernmental competition requires clear assignments, product and factor mobility across jurisdictional boundaries, hard budget constraint and institutional authority. Hierarchical nature of governments helps to deal with externalities. Fiscal autonomy in the assigned jurisdictions means that they cannot create money, access unlimited credit, or get bailouts from higher-level governments in times of fiscal distress. Clarity in assignments is like ensuring property rights; it is necessary both for accountability and incentives. Ensuring a common market makes subnational governments *de facto* "national governments" and increase penalties for protectionism and rent seeking. Internal trade barriers short-circuit inter-jurisdictional competition.

Applying the concept of “soft budget constraint” which was introduced to describe the behaviour of State–owned enterprises in socialist economies, to the subnational governments looking for fiscal relief from the Central Government, Weinghast argues that perverse fiscal behaviour is essentially built into the system. Therefore, the solution to the problem involves a fundamental reform of political and fiscal institutions to alter the structure of incentives in budgetary decisions. Credible commitment to avoid fiscal bailouts is critical to ensuring hard budget constraints. This also requires politically strong Central Government which is not constrained by the States’ bargaining strength to bail them out in times of distress.

Weinghast’s formulation of MPF goes a part of the way in removing the assumption of selflessness in pursuing welfare gain. However, the five preconditions required in this formulation can not be found in the real world. Furthermore, actual conditions in a federal system are governed by political decentralisation and given that fiscal federalism is a component of federalism, it is not clear whether the objective function of individual agents is guided by self motivation. Under the circumstances, it is doubtful whether the governments in general and federal governments in particular can be appraised in terms of their commitment to preserving markets. Assuming that any country can carry out non-market responsibilities such as differential treatment of different groups (racial, linguistic, gender, regional) of population and

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*I am grateful to Albert Breton for drawing my attention to the various implicit assumptions of MPF formulation.*
undertake other functions such as national unity, poverty, education, health, environment, culture and arts in ways without constraining the market preservation would be unrealistic. Equally important, the resolution to the difficult problem of assignment of powers under MPF is a matter of definition. Again, by definition, vertical competition among various jurisdictional levels under MPF can not exist. It must also be noted that in the MPF as in the Tiebout (1956) model, federations are conceived to be two-tier structures. In the latter, national structure is passive so that inter-jurisdictional competition can be precisely defined. However, in MPF, the national tier is not passive, but not active either.

(ii) Competitive Federalism:

Another branch of literature under the SGT brings out the gains from intergovernmental competition in a decentralised system. Brennan and Buchanan (1980) favour decentralisation as the States compete with the Centre and among themselves to provide a check against the government from becoming a “Leviathan”.

In Market promoting Federalism (MPF), analysed above, the subnational governments compete to provide enabling environment for businesses. In terms of conceptual clarity, Breton’s construct of “competitive federalism”, provides a more comprehensive representation of the third strand of literature under the SGTs. Breton (1995, 2006) and Salmon (1987, 2006) provide a more systematic work on vertical and horizontal competition to conclude increase in efficiency under decentralisation. Salmon’s analysis of horizontal competition shows that citizens of a jurisdiction can use information about the public services provided elsewhere to evaluate the performance of their own governments, in the manner of a rank order tournament. Therefore, competition among governments not only affects policies to attract or keep citizens happy, but it also interacts with electoral incentives. Accordingly, “[e]ach government has an incentive to do better than governments in other jurisdictions in terms of levels and qualities of services, of levels of taxes or of more general economic and social indicators.” Empirically, whether this happens (and this is a question that needs to be examined in the Indian context) depends on “the possibility and willingness of citizens to make assessments of comparative performance...and [on] the impact these assessments have on the well-being of politicians” (Salmon, 1987, p. 32). Breton (1995, p. 237) argues that the “Salmon

\[\text{In general incentive models, incentives are not perfect from the principal's point of view because the performance of the agent (here the government) is subject to noise. Hence, performance is not a perfect indicator of effort. Relative performance can help to reduce this noise in evaluating effort: see Milgrom and Roberts (1990), chapter 7.}\]
incentive mechanism” is an essential pre-requisite for competitive governments and is quite important in understanding the diffusion of policies and programs among jurisdictions in federations.

There is considerable overlap between the MPF and Breton’s concept of “competitive governments” discussed above, with different relative emphases on government-market boundaries. Indeed, there are differences in the way in which competition between subnational governments is analysed and the incentive structures exist between different levels of government. As mentioned earlier, the Weinghast’s MPF implicitly assumes the existence of two levels of government. Furthermore, Weinghast’s concept of MPF misses an important point that when there are extreme inequalities in economic power among subnational governments, the efficient solution that is presumed to result from fiscal federalism due to unfettered intergovernmental competition may not realise. This is however, captured in the “competitive equality” of jurisdictions requirement in competitive federalism.

(a) The Rationale for Intergovernmental Transfers:

The assignment system in the normative framework necessarily results in vertical imbalances. Assignment, according to comparative advantage implies that all broad based taxes are assigned to the Centre and most expenditure functions are assigned to subnational levels. Thus, redistribution and stabilization functions are considered to be mainly the functions of Central Government and therefore, all broad based and redistributive taxes, money supply function and borrowing powers are predominantly assigned to the Centre. At the same time, in order to cater to diversified preferences in the provision of public services, the allocation function which involves spending is predominantly assigned to subnational governments. In this scheme, vertical imbalance is unavoidable and the intergovernmental transfer system has to resolve the imbalance. At the same time, it is important to match the revenue and expenditure decisions at the margin for subnational governments for reasons of efficiency and accountability. The efficient system of tax assignment envisages that tax powers should be assigned to subnational levels up to the point where the marginal efficiency loss due to tax disharmony is matched with marginal efficiency gain from fiscal autonomy. Even with such an assignment system, vertical imbalance is a feature seen in all federation.

The rationale for horizontal transfers in this case is purely for equity reasons - to offset the fiscal disabilities arising from lower than prescribed revenue capacity and higher unit
cost of providing public services. Differences in the capacity to raise revenues and unit cost of providing public services among subnational jurisdictions create different ‘fiscal residuum’ or net fiscal benefits (Buchanan, 1950). The problem is exacerbated when there are origin based taxes and similar other factors alter the net fiscal benefits in different subnational jurisdictions (Boadway and Flatters, 1982). If there is perfect mobility of people across jurisdictions, fiscal differentials will be equalized automatically as people migrate from places where the net fiscal benefits are lower to those where they are higher. Even when there is no perfect mobility, if the property market is reasonably well developed fiscal differentials will be capitalized into property values (Oates, 1969). In developing countries, there is neither perfect mobility nor a developed property market and the only way left is to offset these fiscal disabilities arising from low revenue capacity and high unit cost of providing public services through intergovernmental transfers. Such transfers have to be necessarily unconditional – to enable every State to provide a standard level of public service at a normative tax rate.

Efficiency consequence of equalizing transfers has been a matter of considerable debate in the literature. The debate on the issue of whether the horizontal equalization transfers are efficiency enhancing or involve efficiency cost is an issue that has remained unresolved. While Buchanan (1950) and in the later formulation based on horizontal equity argument by Boadway and Flatters (1982) argue that equalising transfers are growth enhancing. Similarly, the competitive federalism literature recommend transfers to create a level playing field by enabling poorer jurisdictions to compete effectively with fiscally stronger ones (Breton, 1987). Buchanan’s claim is that equitable transfers are also efficiency enhancing because, as capital-labour ratio in these regions is lower, the productivity of capital is high and transfer of capital to poorer regions would lead to higher productivity and incomes.

The view that equitable transfers to poorer regions are growth enhancing is not shared by many. The contrarian view is that there is a clear trade off between equalization and growth. Scott (1950) argues that income levels in poorer regions are low mainly because of lower productivity and transfer of capital to these reasons will entail lower productivity and incomes and there is clearly a tradeoff between equity and efficiency. Despite a large volume of literature, whether or not there is equity – growth trade off in the case of equalising transfers remains theoretically unresolved and remains an empirical issue. The transfers can help to realise the growth potential of the locality by creating the necessary infrastructure or it may actually be used to impart skills to labour, enhance productivity and accelerate mobility of labour from regions having surpluses. In any case, the practice
of giving equalising transfers is in the realm of history, tradition and political economy and countries such as Australia, Canada, India and Germany have been giving such transfers whereas, the United States does not.

There is a case for transfers also to ensure that people are provided with minimum standards basic services with significant inter-jurisdictional externalities. The efficiency reason for intergovernmental transfers arises from spillovers. The assignment system, however well done, does not match with the geographical boundaries of the jurisdictions and spillovers have to be resolved thorough the transfer system. There are also services which must be available at minimum specified standards to all and these include minimum standards of education, healthcare, water supply and sanitation. Martin Feldstein calls them “categorical equity” goods (1975) as these services have nation-wide externalities and yet, subnational governments have a comparative advantage in providing them. In respect of all these services which overlap jurisdictions and involve significant externalities, it is necessary to ensure minimum levels for reasons of efficiency.

Ensuring minimum levels of public services for externality reasons is best done with a system of open ended matching grants. The extent of matching by the higher level government is supposed to reflect the degree of externality and open-endedness is necessary to provide incentives of expansion of the service at the margin. In practice, however, the matching ratios do not have any relationship with the extent of externality and in most cases, multiplicity of shared cost programmes and the resource constraint at the Central level results in making such programmes closed ended, but such programmes do not provide the incentive for expansion at the margin. In many cases, both the matching ratios and the volume of transfers is determined not on the basis of the externalities but simply for political reasons.

Using a collective choice framework, Bradford and Oates (1971) showed that lump-sum grants to a group of persons would have identical allocative and distributional effects to a set of transfers directly given to individuals in the group. In other words, the lump sum grants to a group of persons would be simply a “veil” for a central tax cut to individuals in the group. However, empirical analysis has not provided any support to this “veil hypothesis”. In contrast, empirical analyses show that lump sum grants result in the expansion of public spending rather than private incomes and this has come to be known as “flypaper effect”. There is a large body of literature in the US that tries to explain this empirical fact (Gramlich, 1977). Indeed, in a situation where subnational governments
raise very little revenues through taxes like in the case of local governments in India, the possibility of substituting own taxes to transfers simply do not exist and the hypothesis itself does not make much sense.

In the actual design of the transfer system, there are serious operational questions, which can not be resolved easily. The first has to deal with the proper combination of conditional and unconditional transfers. The second issue has to deal with the extent of horizontal and vertical distribution. There is no unambiguous way to measure the degree of vertical imbalance and the extent of violation of horizontal equity. As regards specific purpose transfers are concerned, it is impossible to measure the degree of externalities to work out optimal cost sharing arrangements or matching ratios. Ironically, the very argument for decentralisation is based on asymmetric information or the inability of the Central Government to estimate the correct degree of spillovers, but designing specific purpose transfers requires that the matching ratios will have to be determined according to the degree of externalities! Finally, even if some approximations on fiscal disabilities and matching ratios made, there are many non-economic including political objectives and the actual transfer system, differs from the ideal. Nevertheless, the attempt should be to approach the ideal both in designing it and in its evaluations.

Are intergovernmental transfers a good idea? Despite the rationale for transfers detailed above, the review of theoretical literature shows that transfers tend to soften the budget constraint of subnational governments. It shows that intergovernmental grants promote fiscal irresponsibility and macroeconomic instability (Prud’homme, 1995). It is also argued that equalization may actually impede the development of backward regions by preventing the inter-regional mobility of resources, particularly labour (both emigration and immigration) in response to cost differentials (McKinnon, 1997). They create “transfer dependency” (Rodden et.al., 2003), which undermines fiscal discipline. Even in the case of matching transfers, in which matching ratios should be worked out according to the extent of spillover, Inman’s (1988) study in the U.S. found that in actual practice, the matching ratios never correspond to the extent of spillovers and the federal share is invariably much higher than the spillovers involved. Even more serious are the objections raised on equalising transfers given in many federations (the notable exception being the USA). It is argued that the transfers given to offset fiscal disadvantages can interfere with the normal process of income convergence seen in the process of economic growth which occurs due to migration of labour and capital from places with lower productivity to those with higher productivity.
The above analysis casts serious doubts on the efficacy in intergovernmental objectives in serving the long term interests of a federation. Nevertheless, transfers are a part of every federation because, perfect matching of revenue powers with expenditure responsibilities is not possible. Nevertheless, the literature provides guidance on a number of issues relating to transfers. First, the role of transfers should not be so large as to create transfer dependency. There has to be a matching of revenue and expenditure decisions at the margin so that decisions on additional spending are matched by financing it through taxation (Bird and Vaillancourt, 1998). Second, the system of grants must be transparent and predictable and should not have incentives to free-ride. Surely, designing and implementing the transfer system is the most important issue in fiscal federalism.

(d) Key Determinants of Successful Fiscal Federalism:

The preceding analysis helps us to identify the factors determining the success of a federation in terms of achieving economic prosperity and reducing poverty while retaining individual identities and receiving the public services closely matching the diversified preferences. In other words, there are important preconditions to be met if a federation has to benefit from its magnitude (largeness) and littleness as Alexis de Toquelle asserted over a hundred years ago. Besides, these theoretical approaches provide a number of lessons.

It must be noted that the theories of fiscal federalism reviewed above do not distinguish between different multilevel fiscal systems. The theories have been developed irrespective of the number of level and the size of jurisdictions. Indeed, each public service would have its area of benefit span and it is not possible to have as many tiers as the number of public services provided. Therefore, aggregation of public services within the limited number of jurisdictions is unavoidable and with this spillovers and efficiency concerns become a part of the fiscal federalism problem. The type of problems faced in the provision of public services by different tiers could be different, but the theoretical approaches do not distinguish between them. Thus, it would be inappropriate to consider the challenges faced by the state governments to be similar to those faced by the local governments, the types of public services provided, the method and the nature and quality of institutions and their capacities are vastly different.

One of the most important preconditions for a successful fiscal federalism is clarity in the assignment system. Not only that the assignment system should be clear as far as possible, but when there is overlapping, there should be systems and institutions to deal with it. Clarity in assignments does not only imply mere assignment of revenue and expenditure
powers; it is also necessary to ensure that the functions of different functionaries within a level are unambiguous. In a democratic polity, it is necessary to make the elected representatives responsible for decision making and bureaucrats to implement the decisions taken by the executive.

According to the theory, the functions should be assigned according to comparative advantage and the financial powers should follow the functions specified. It is important to ensure that the subnational governments are not constrained by transfer dependency. Ensuring a strong “Wicksellian link”, - the linkage between revenue and expenditure decisions at the margin requires that the subnational governments are given adequate revenue powers. Accountability requires that subnational services should be paid for by the residents of the jurisdiction. The analysis of appropriate revenue handles at subnational levels shows that user charges should cover the cost of most private goods provided by them; the cost of public services benefiting the jurisdiction should be collected by way of taxes on the residents; and those with spillovers should be partly paid for by taxes on the residents (equivalent to the benefits received by them) and partly through intergovernmental transfers. Analysis also shows that the subnational governments can levy taxes on immobile bases and can levy taxes on mobile bases based on the benefit principle. However, taxing mobile bases could prove to be ineffective in raising revenues besides transferring the burden to non-residents.\textsuperscript{10}

The transfer system should address the problem of imbalance between revenue and expenditure powers. To enable every governmental unit to provide comparable levels of public services at comparable tax rates, it is necessary that the equalising transfer system is designed to offset fiscal disadvantages. At the same time, it is important to ensure that the subnational governments are not provided with the incentive to “raid the fiscal commons”. Ensuring proper incentive structure in the transfer system is critical to preventing the soft budget constraint. It is necessary that the states are not enables to pass on the burden of their public services to non-residents through the transfer system. In addition to equalization transfers, specific purpose matching (open ended) transfer should be designed to compensate the public services provided by the subnational governments the benefit of which spill over the jurisdictions and the matching ratios should be equivalent to the extent of spillovers. However, measurement of spillovers is

\textsuperscript{10} For a detailed analysis of appropriate tax handles see, Bird and Slack, 2007 and the analysis in the context of Australian federation, Bird and Smart, (2009).
not easy and therefore, these transfers are hardly designed to offset the spillovers. Besides, in most cases, the transfers are never properly designed.

A major advantage of a multilevel fiscal system is the large common market, but the benefit can accrue only when not only all impediments to trade in factors of production as well as commodities are removed, but also mobility of commodities, capital and goods is facilitated. Ensuring a common market is at the heart of creating dynamism in fiscal federalism. The impediments can come in terms of policies restricting the movement of labour, capital and commodities or various institutional factors such as linguistic barriers and lack of secure environment. The literature on MPF shows that it is important to avoid soft budget constraint at subnational levels to ensure efficient and market friendly policies. This requires an efficient assignment system, policies to promote responsible fiscal behaviour and measures to strengthen and deepen the markets, particularly the land and capital markets. Removal of impediments to mobility and trade in factors and products include abolition of laws restricting the markets and removal of institutional rigidities.

There can be gains from intergovernmental competition. Competition can lead to efficiency gains in public service provision; it can also motivate innovations and productivity increases in public service delivery. However, to reap the gains, it is important to ensure that there is a measure of competitive equality and predatory competition does not take place. Unequal competition could be destabilizing and can, in the extreme, break up the federation. This is particularly important in the context of globalization as the States with more developed markets and infrastructure can reap higher benefits from access to domestic and international markets and grow faster than those with less developed markets and infrastructure. To ensure a measure of competitive equality of jurisdictions, it is necessary to ensure that the combined impact of regional policies and intergovernmental transfers should ensure a defined standard of physical and social infrastructure in each jurisdiction and the transfer system and the transfer system is not subjective and discretionary.

The analysis brings out the need for strong systems and institutions to promote and regulate efficient competition. One method to deal with the problems of predatory competition is centralization, but that would tantamount to ‘throwing the baby with the bath water’. The argument for decentralisation in the first instance is to create a system to take advantage of lower information and transaction costs in public service delivery and, therefore, this
can not be a viable solution. The solution has to be found within the decentralised framework to create institutions to bargain and resolve inter-State and Centre-State conflicts.

Some of the important features of strong institutions for creating hard budget constraints emerge in a well developed market economy. Efficient credit markets and a mature banking system and well developed debt market with developed credit rating institutions is an important precondition for the Centre to keep itself away from bail outs. Similarly, well developed land and property markets and efficient mobility of factors and products can prevent public decisions that impede the development of markets. These will promote intergovernmental competition and minimize incentives for bail outs. It is important to discourage protectionist policies at subnational levels. Equally important is the need to have strong fiscal institutions. Effective local system of taxation, to match revenue – expenditure decisions at the margin, and the efficient system of intergovernmental transfers which do not involve perverse incentives are extremely important to ensure a hard budget constraint. Legislatively imposed constraints on deficits and requirement to balance the current budgets, will place a limit on fiscal expansion and ensure more productive public spending. Limitations placed on borrowings both internally can also help to contain perverse incentives for fiscal expansion. It is also necessary to have a well designed bankruptcy laws that specify the fiscal crisis and the way that needs to be handled is another important institutional requirement. Indeed, the type of systems and institutional developments to encourage efficient and regulate inefficient competition and to ensure hard budget constraints will have to be found according to the requirements of each country.

Often arguments are made for centralization on the grounds that technological improvements have reduced the information cost and asymmetry and it is possible for the Centre to design and implement the programmes according to diverse preferences. Indeed, it is important to use the technology if it helps efficient provision of public services without sacrificing the capacity to cater to preference diversity. Sometimes, the arguments for decentralisation is actually for privatization and in such a case, simply decentralizing the supply may not yield the desired results (Tanzi, 2002). It is therefore, important to examine the case for decentralisation in each case and judge it based clearly on efficiency grounds.

Australian federation, Bird and Smart, (2009).
From the above discussion, it is clear that much of the theoretical literature on fiscal federalism has been modeled on western democracies having mature market economies. There are a variety of reasons to modify the mainstream fiscal federalism analysis before it is applied to the multilevel fiscal systems in developing and transitional countries (Rao., 2007). This is because developing countries have a predominant primary sector, coexistence of a large traditional sector with low market penetration and a small modern sector which links itself with the market. It has segmented labor markets, low level of savings and investment, large part of the savings in physical rather than financial assets. There is imperfect mobility of labour, competition with significant trade distortions and scarcity of foreign exchange. The adoption of planned development strategy in them has further distorted the markets (Newbery, 1987). Secondly, most of these economies have adopted centralised planning in a decentralised system. In India, in addition to all these, the development strategy has adopted the mixed economy framework. Even as most countries have chosen to make a transition from centralized planning to market based resource allocation, the vestiges of planning continue to influence resource allocation outcomes. Developmental planning adopted by developing countries in the past and the vestiges of centralised planning in the economies making a transition from plan to market do influence the fiscal federalism outcomes and therefore, need to be analyzed in greater detail. In most such economies, several impediments to the movement of factors and products continue. Similarly, as a part of planning system, controls and prices and outputs continue in many countries in transition and this alters the allocation of resources and determines incomes in different regions in unintended ways. As Stated by Oates (1999, p. 1145), “While the existing literature on fiscal federalism can provide some general guidance, …my sense is that most of us working in the field feel more than a little uneasy when proffering advice on many of the decisions that must be made on vertical fiscal and political structure. We have much to learn”.

Theories of Fiscal Federalism: A Review
Evolution of Indian Fiscal Federalism

(a) Historical factors:

Indian fiscal federalism, over the last 60 years has undergone considerable changes. While some of the developments have helped it to cement the country to emerge as a nation, there are others which threaten to destabilise it. In this section, the evolution of Indian fiscal federalism is analysed in the light of the theoretical literature reviewed in the previous section. In particular, the review of FGT and SGT in the previous section provides us a framework for evaluating the policies and institutions in Indian fiscal federalism.

In a liberalized, open market economy, the federal fiscal policies and institutions have important roles to play in creating an enabling environment to accelerate growth and reduce poverty. These include, facilitating unencumbered mobility of factors and products, designing and implementing a harmonious and efficient tax system which minimizes the collection, compliance and distortion costs while generating the required revenues, ensuring competitive standards of social and physical infrastructures and effect their even regional spread and creating administrative, political and fiscal institutions to ensure proper structure of incentives and accountability at both national and sub-national levels.

There is considerable debate as to whether Indian fiscal system should be considered federal at all. The strong centripetal bias in the Constitution has made many astute observers to designate India as “quasi-federal”. The Constitution of India characterizes India as a “Union of States” and not as a “federation”. India does it fit into Kenneth Wheare’s characterization of federalism in which the subnational units should be “co-ordinate and independent”. Indeed, there are few countries in the world in which the sub-national governments would qualify the test of being “co-ordinate and independent”. As indicated in the previous section, we are concerned in this paper about the functioning of Indian fiscal and not political federalism. Furthermore, India passes Breton’s test of having sufficient checks and balances to prevent extinction or even curtailment of the powers of the States and therefore, qualifies for being labeled as federal. Nevertheless,
the extent of centralization inherent in the Constitutional division of powers and the way in which the intergovernmental relationships have evolved over the years shows that the highly centralised nature of Indian fiscal federalism needs to be reformed in order to make it responsive to the needs of liberalized economy with outward orientation.

Indian fiscal federalism has constitutional demarcation of functions and sources of finance between the Union and the States. However, unlike a classical federation in which confederating units join to form a common market evolving into an economic and political union, Indian federation was formed mainly from the unification of the principalities in British India and after independence, accession of the remaining princely States to the Union. The one billion people in the federation are spread over twenty-eight States and seven centrally administered territories (two with their own elected governments). Separate legislative, executive, and judicial arms of government are constituted at both Union and State levels. The upper house, or Rajya Sabha, in the Parliament is the House of States, to which members are elected by an electoral college from each of the States. The Seventh Schedule to the Constitution specifies the legislative domains of the Union and State governments in terms of Union, State, and Concurrent lists. The Constitution also requires the President of India to appoint the Finance Commission every five years (or earlier) to review the finances of the Union and the States and recommend devolution of taxes and grants-in-aid for the ensuing five years.

Historical factors have played an important part in the adoption in India of a federal Constitution with strong unitary features. During the British rule, administrative and fiscal centralisation was a colonial imperative. At the same time, the difficulty of administering a large country with a number of principalities, divergent languages, cultures and traditions did call for some degree of decentralization. Indeed, for a period of about two decades in British India prior to the enactment of the Government of India Act 1935, the system required the provinces to make a contribution to the Union. Although there were strong arguments for decentralisation before independence, and even though the Cabinet Mission sent by the imperial government envisaged limited powers for the Union in a three-tiered federal structure, the constitution that was eventually adopted by the Indian Republic closely followed the Government of India Act, 1935, with pronounced “quasi-federal” features. The shift probably occurred for two reasons: First, once the Muslim majority areas opted out of India to form a separate country, the principal rationale for a loose federal structure no loner existed. Second, a strong Centre was found desirable to safeguard
Evolution of Indian Fiscal Federalism

against fissiparous tendencies among constituent units (India, 1968, Chelliah, 1991) particularly, the erstwhile princely States. The federal framework provided by the founding fathers of Indian Constitution was an experiment in adopting the federal idea to a large and extremely diverse economic, cultural, social, and linguistic society.

The Indian Constitution promulgated in 1950 was erected on the foundation provided by the Government of India Act, 1935. While most of the provisions of the Act were copied on to the Constitution, it incorporated new ideas of fundamental rights from the American Constitution to guarantee the citizens justice, liberty, equality and fraternity. It also defined the Directive Principles of State Policy borrowed from the Irish Constitution and brought in the concept of responsible government and accountability of the executive to the legislature based on the unwritten conventions of the United Kingdom. The heavy reliance on the 1935 Act was justified on the grounds of “continuity and harmony” (Chanda, 1965). Consequently, many important features of the Act including its strong centripetal bias and administrative and judicial arrangements enacted for limited purposes of colonial administration were formally incorporated into the Constitution. Thus, instead of conceiving federalism as autonomous States coming together, it was an arrangement for the continuation of the unitary form of government with greater devolution. Thus, the legislative, administrative and fiscal relationships designed in the new set up were merely an extension of the existing arrangements.

The Constitution of the Indian Republic, like the 1935 Act, provided the three-fold distribution of powers (Article 246). It transferred a few minor items from the Central List to the Provincial List and vested greater powers to the Central Government in certain other spheres like national highways, inter-State trade and commerce to foster national economic unity and promote a common market. Although not explicit, the matters of national importance were assigned to the National Parliament or the Union List (List I) and those of regional importance were assigned to State Legislature and placed in the State List (List II). Those matters relevant to both the Parliament and Legislatures were listed in the Concurrent List (List III). The attempt, like the 1935 Act was to assign the functions to the two levels based on their comparative advantage in carrying them out and achieve mutually exclusive divisions to avoid overlapping. However, functions in which both the levels of government had a stake were placed in the Concurrent List. The residuary powers were reserved for the Union government.
(b) Centralization in Indian Fiscal Federalism

(i) Constitutional Assignments:

The constitutional division of legislative powers between the Union and the States has been a subject matter of considerable debate. Besides the official reports of the Finance Commissions, Administrative Reforms Commission (India, 1969), the study team report on Centre-State relations appointed by the Government of Tamil Nadu and more recently, by the Commission on Centre-State relations (India, 1988), a number of scholars have discussed various aspects of the assignment system in the Constitution and notably the intrusion of the powers of the States by the Centre over the years.\(^\text{11}\)

As elaborated by the Administrative Reforms Commission, the “classical federalism” as stated by Wheare (1963) presupposes that the units should be coordinate and independent. This implies:

(i) a contract between independent and sovereign units surrendering their partial authority in pursuit of common interest;

(ii) the residual authority residing with the constituent units;

(iii) a separate constitution for each of the constituent units to govern on matters that are not surrendered to the Union;

(iv) the supremacy and immutability of the constitution except with the concurrence of the constituent units;

(v) the distribution of powers of the Union and the constituent units each in its sphere, co-ordinate and independent of the other; and

(vi) the supreme authority of the courts to interpret the constitution, to resolve conflicts between the Union and the States and among the States inter se.

Only the last item of the classical federalism is applicable to Indian situation. The constituent units in Indian situation do not have a constitution of their own; they do not have political sovereignty either; nor are they coordinate and independent of one another. The Constitution that was evolved in the Indian context was, therefore, described as a ‘quasi-federal’. In fact, in its final report to the Constituent Assembly (August 20, 1941), the Union Powers Committee Stated: “We are unanimously of the view that it would be

\(^{11}\) There is a large body of literature on Centre-State relations, mostly descriptive on this issue. See, Rao and Chelliah (1996), Gulati and George (1985), Vithal and Sastry (2001) and Chelliah (1991).
injurious to the interests of the country to provide for a weak Central authority which would be incapable of ensuring peace, of coordinating viable matters of common concern and of speaking effectively for the whole country in the international sphere” (quoted in Sarkaria Commission Report, p.7).

Thus, India evolved as a two-tier fiscal federalism until the 73rd and 74th Amendments to the Constitution recognised the third tier of government below the State level in rural and urban areas. The Seventh Schedule to the Constitution assigned the legislative domains including the functions and fiscal instruments to carry out the functions for the Union and State governments. The Constitution recognises that there would be imbalances between the revenue powers and expenditure responsibilities at Central and State levels and provides for a mechanism for resolving this vertical fiscal imbalance. The Constitution also provides for the setting up of the Finance Commission every five years or earlier to make recommendations on the proportion and the principles for the distribution of Central taxes to be shared with the States and among the States inter se. In addition to the tax devolution, the Finance Commissions are required to make recommendations on the grants-in-aid to be given to each State, augmentation of consolidated funds of the States to assist the rural and urban local bodies consequent to the 73rd and 74th Constitutional Amendments based on the recommendations of the State Finance Commissions and on any other matter entrusted to the Commission by the President of India in the interest of sound finance.

Consequent on the 73rd and 74th Constitutional Amendments, two separate schedules were inserted into the Constitution listing the functions to be assigned to rural and urban local bodies. With this, separate Schedules – 12th and 13th – listing the 29 and 18 functions respectively for rural and urban local bodies are listed and these functions are to be devolved to them. These functions are to be undertaken by the rural and urban local governments concurrently with the State governments and the extent of devolution would be done by the State governments at their discretion. The State governments are also required to appoint a State Finance Commissions every five years to assess the requirements of the rural and urban local bodies and recommend transfers to them. The Union Finance Commission has been assigned the task of “augmenting the consolidated funds of the States” consequent upon 73rd and 74th Amendments to the Constitution based on the recommendations of the State Finance Commissions. Furthermore, the rural local bodies and urban local bodies, besides being units of governance are also conceived to be institutions to undertake grass-roots planning and the planning process is supposed to be coordinated at the district level by the District Planning Committee.
(ii) **Centripetal Bias in the Constitution:**

The centripetal bias in Indian fiscal federalism comes out clearly in a number of articles of the Constitution. Although the assignment broadly are in line with the pattern in most other federations with most functions relating to defense, macroeconomic management of the economy, significant redistribution and allocation functions involving significant scale economies and pan State geographical spread are assigned and those functions relating to the provision of public services within the State jurisdictions are assigned to the States. Thus, the Centre has exclusive jurisdiction over defense, atomic energy, space, foreign affairs, macroeconomic management of the economy, communications and those services involving inter-State ramifications while the States’ domain comprises of public order, public health, water supply and sanitation, irrigation, industries excluding those declared by Parliament to be of strategic interest.

There are several pronounced unitary features in Indian Constitution which raises serious questions on the scope for the subnational governmental units to play important roles in the development of the country. Some of these are summarized in the following:

(i) Article 3 of the Constitution which allows the Centre to alter geographical boundaries of the State, change their names, carve out new ones from combining parts of one or more States after merely referring the bill providing for such alteration or annihilation to the Legislature of the States concerned for expressing their views.

(ii) Article 249 empowers the Rajya Sabha (Council of States) to transfer any item contained in the State List of 7th Schedule to the Union List with two-thirds of the members present and voting, if it is thought to be expedient in the national interest to do so. Given the fact that the political parties in India do not have a federal character, it would be unrealistic to expect the Rajya Sabha to protect the interest of the States.

(iii) Article 250 empowers the Parliament “… to make laws for the whole or any part of the territory of India with respect to any matters enumerated in the State List” when emergency is proclaimed.\(^{12}\) Further, after the emergency has

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\(^{12}\) Article 352 provides that if the President is satisfied that there is a grave danger for security of India or in any part of the country is threatened by external aggression or internal disturbance, he can proclaim emergency. When emergency is proclaimed, the Fundamental Rights under Article 19 remain suspended.
ceased, the law passed by the Parliament even if is outside its competence can continue to function for a period of six months. This is supplemented by Article 353 (b) which empowers the Union government on matters outside those enumerated in the Union List. Also, the President can, under Article 354, suspend the provisions of Articles 268 to 279 which deal with the distribution of revenues between the Union and the States while the proclamation of emergency is in operation. The Constitution also envisages the possibility of financial emergency in the States and, in such circumstances, restricts financial authority of the States.

(iv) Although Article 301 guarantees the freedom of trade and commerce throughout the country, Articles 302 and 303 read together empower the Parliament to impose restrictions on internal trade if it is required in ‘public interest’ and is non-discriminatory. ‘Public interest’ is an ambiguous concept which can be prone to subjective interpretation and misuse. In fact, the States have been empowered to levy inter-State sales tax on their exports to other States so long as there is a sales tax on the domestic consumption of the good and this has created serious impediments to internal trade besides creating iniquitous transfer of resources from poorer to richer regions. Similarly, under Entry 52 of the State List, urban local bodies can levy a tax on the entry of goods into a local area for consumption use or sale. The levy of Octroi or Entry Tax under this provision is in the nature of import duty levied by local areas. Besides obstructing free movement of goods, it creates severe distortions. In addition to these, the States can also put reasonable restrictions on trade and commerce with the previous sanction of the President.

(v) The assignment system has a large concurrent list covering wide areas such as “economic and social planning” with residuary powers assigned to the Centre.

(vi) The Constitution lays down the primacy of Central laws in the event of a conflict between a State legislation and a Parliamentary law.

(vii) Article 201 requires State Governor’s assent for laws passed by State assemblies and of President’s assent for State enactments in certain matters.

(viii) The most serious violation of federal principle, however is implicit in Article 356, which provides that:

“If the President, on receipt of a report from the Governor of a State or otherwise, is satisfied that a situation has arisen in which the government of a State cannot be carried
on in accordance with the provisions of the constitution, the President may by proclamation:–

a) assume to himself all or any of the functions of the government of the State and all or any of the powers vested in or exercisable by the Governor … or any body of authority in the State other than the Legislature of the State;

b) declare that the powers of the Legislature of the State shall be exercisable by or under the authority of Parliament;

c) make such incidental and consequential provisions as appear to the President to be necessary or desirable for giving effect to the provisions for suspending whole or in part the operation of any provisions of this Constitution relating to any body or authority in the State…”.

These provisions are extraordinary; they not present in any other Constitution (Chanda, 1965, p.100) and find their genesis clearly from the Government of India Act, 1935. Although the provision is meant to be invoked under extraordinary conditions of Constitutional breakdown, it has been subject to widespread misuse, particularly since 1966. The Commission on Centre-State Relations (1988) after a thorough analysis of 84 cases of invoking this article from 1950 to 1987 concluded that in 58 cases the use of the provision was ‘clearly unjustified’. Such cases consisted of not only the attempts by the ruling party at the Centre to deny the opposition parties to form or continue in power, but also has been used by the ruling parties at the Centre to settle factional squabbles within their parties”.

(c) Centralising trends in the functioning of Fiscal Federalism:

The centralisation inherent in the constitutional assignments was accentuated by the working of the fiscal federalism over the years. The item “social and economic planning” in the concurrent list provided tremendous scope for centralisation of economic powers and with the adoption of planned development involving public sector dominated, heavy industry based, import substituting industrialisation strategy, the Central Government acquired the powers to allocate resources of the country. As noted by Chelliah (1991), “Centralised planning is negation of federalism” and the planning process enormously curtailed the powers of the subnational governments.

Allocating resources according to plan priorities called for introduction of several controls and regulations on both financial and real sectors of the economy. On the real sectors,
various controls had to be exercised on both prices and output and in several sectors, administered pricing mechanism virtually replaced the market and in fact, constrained the development of the market altogether. As the private sector investment had to be channelised according to plan priorities, industrial licensing system and a variety of other controls had to be put in place. To prevent monopolistic practices of the private industry getting licences, various other legal and regulatory restrictions besides extortionary tax policy had to be introduced which resulted in significant disincentives to work, save and invest. Even after market based reforms were introduced in 1991, the vestiges of planned development and centralisation inherent in the system have continued.

Financing the large public sector required resource mobilisation and the tax policy had to be geared to undertake the task. Thus, taxes had to be raised to raise revenues without much regard to their economic consequences. The restrictions on the financial sector had to be placed to ensure allocation of financial resources according to plan priorities. Financing the plans had to be done predominantly from domestic savings and this required the transfer of household savings to the public sector and that necessitated the policy of financial repression. The scarcity conditions prevailed at the time of independence exacerbated by periodic droughts required the government to introduce rationing and several controls and restrictions on the movement of essential commodities. All these concentrated economic as well as administrative powers in the hands of the Centre (Chelliah, 1991).

The most important development that led to significant centralisation - almost as much as what the planning process did - was the nationalisation of financial institutions and commercial banks. The nationalisation of Imperial Bank of India to create the State Bank of India in 1947 and the Life Insurance Corporation of India in 1956 was to ensure allocation of resources according to plan priorities. The subsequent nationalisation of important commercial banks in 1969 was a political decision, though the ostensible reason that the social control of the banks failed in the social obligations of reaching the farmers and other disadvantaged sections of society. The nationalisation of the banking system vested the virtual control over the financial system to the Central Government.

In a number of areas, centralization was achieved by the Central Government intruding into the States’ domain either by transferring the subjects in the State List to the Concurrent

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13 The move coincided with the wresting of the power by Mrs. Indira Gandhi from the older leaders. The nationalisation of 14 major commercial banks was a clever move as it helped Mrs. Gandhi to consolidate power with the support of the Communist Party of India.
List (for example, education and forestry) or expanding the scope of Entry 52 in the Union List to assume control over one industry after another or by creating several ‘institutions of national importance’ to intrude into the areas in the State List, or by influencing the pattern of spending on items in the State List through central sector and centrally sponsored schemes (which are specific purpose conditional transfers). Secondly, interpretation of Art. 282 of the Constitution as a miscellaneous provision and making overwhelming proportion of the transfers for State plan schemes and centrally sponsored schemes has virtually undermined the relevance of the Constitutional scheme for making transfers, namely, Arts. 270 and 275 which is based on the recommendation of the Finance Commission.

This development has led to several undesirable consequences on both public service delivery and systems of accountability. First, the role of the Finance Commission, the Constitutional body meant to recommend transfers has substantially eroded as increasing proportions of the Central transfers to States have become discretionary. Second, large proportions of Central transfers for activities and schemes in the State list are given directly to local bodies and various other implementing agencies bypassing the States. This, besides violating the principle of accountability has made it difficult to take a holistic view of delivering various public services. Third, the entire budgeting system has been segregated into plan and non-plan with each of the spending agencies of the Centre and States taking a partial view of spending on various public services. This has had serious disincentives for adequate provision of maintenance expenditures and even more importantly, poor systems of expenditure management.
Some Salient Features of Indian Fiscal Federalism

(a) Preserving the Common Market

The benefits of “littleness and magnitude” of nations can be realised only when they have a common market with unhindered movement of goods across the federation and unhindered mobility of capital and labour. This would result in the development according to comparative advantage of different regions and maximise the growth of the country. At the same time, it enables competition among jurisdictions which will enhance efficiency in public service delivery and incentivise the subnational jurisdictions to innovate and improve productivity. Promotion of common market therefore, is an essential precondition for reaping potential gains from fiscal federalism. As discussed in Section 2, both MPF and competitive federalism formulations of fiscal federalism underline the importance of ensuring unfettered movement of factors and products across jurisdictions and the need to have hard budget constraints besides clarity in the assignments itself. Indeed this has been the case in the United States since the inception of the Constitution and holds good in many other federations.

In Indian context, interestingly, the framers of the Constitution, although aware of the need to ensure a common market in the federation, were not averse to the idea of placing restrictions if the situation so demanded. Article 301 of the Constitution States, “subject to the other provisions of this part, trade, commerce and intercourse throughout the territory of India shall be free”. At the same time, Article 302 empowers Parliament to impose restrictions on this in “public interest”. This is not surprising because both the general scarcity conditions that prevailed at the time the Constitution was framed, and centralised planning introduced at a time when savings and investment rates were lower than 10 per cent of GDP and the limited availability of foreign exchange available required rationing and restrictions to be placed on the movement of goods as well as allocation of capital across States. Unfortunately, several fiscal and regulatory impediments to internal trade have continued even as the objective conditions have changed over time.
An important fiscal impediment to free inter-State trade is the levy of inter-State sales tax. The tax is levied by the exporting State on inter-State sale of goods. Notably, the founding fathers of the Constitution intended that the sales tax system in India should be destination based. According to Article 286 of the Constitution, “No law of a State shall impose, or authorise the imposition of the tax on the sale or purchase of goods where such sale or purchase takes place (a) outside the State, or (b) in the course of import of goods into, or export of goods out of, the territory of India”. However, based on the recommendations of the Taxation Enquiry Commission (India, 1953), the Sixth Amendment added clauses (2) and (3) to enable the Central Government to levy taxes on inter-State transaction. The clauses read:

“(2) Parliament may, by law formulate principles for determining when a sale or purchase of goods takes place in any of the ways mentioned in clause (1).

(3) Any law of a State shall, insofar as it imposes, or authorises the imposition of,

(a) a tax on the sale or purchase of goods declared by Parliament by law to be of special importance in inter-State trade or commerce; or

(b) a tax on the sale or purchase of goods, being a tax of the nature referred to in sub-clause (b), sub-clause (c) or sub-clause (d) of clause (29-A) of Article 366; be subject to such restrictions and conditions in regard to the system of levy, rates and other incidents of the tax as Parliament may by law specify”.

Under these provisions, the Central Government has authorised the States to levy the tax on inter-State sale subject to a specified ceiling rate. Besides creating impediment to free movement of goods (through check-posts), this tax on export of goods from one State to another has converted the sales tax into a partially origin-based tax and this causes significant inter-state tax exportation from rich exporting States to poor importing States (Rao and Singh, 2005). The tax has also has caused significant inter-State exportation of the tax burden from the richer producing States to the residents of poorer consuming States. As a part of the reform to transform the sales tax into a destination based value added tax (VAT), the rate has been reduced from 4 per cent to 3 per cent in 2007-08 and further to 2 per cent in 2008-09. With the levy of Goods and Services tax (GST) in the country, it is hoped that a technological solution to trace inter-State transactions will replace the central sales tax. In other words, computerised information system to track inter-State transactions will obviate the need for taxing inter-se sale or the need to place impediments on the movement of goods across the country.
Another fiscal impediment to free movement of goods is in the form of tax on the entry of goods into a local area. Although Article 286 does not impose restrictions on inter-State transactions, entry 52 in the State list empowers the States to levy tax on the entry of goods into a local area for consumption, use or sale. In many States, the tax has been assigned to the urban local bodies and the tax is variously called, “octroi”, or “entry tax”. Thus, the tax is levied not only on the exports from one State to another but also on all imports into local areas including imports from other States. These taxes have complicated the tax system, created severe distortions, caused severe impediments to inter-regional movement of goods, increased the compliance cost substantially and factors and have been a source of corruption. Almost all the States which were originally levying the tax have abolished it and Gujarat, the last State to abolish the tax even in the municipal corporations has tried to raise compensating revenue by levying an additional percentage point tax rate on the value added tax. Maharashtra is the only State where the tax is still levied by the municipal corporations.

In addition to the fiscal factors, there are several regulatory policies violating the principles of a common market. These have been introduced as a part of the planned development strategy or as a part of supply management to meet scarcity conditions. While many of the regulations restricting the free flow of goods and factors of production have been removed, the consequences of past policies continue to distort resources as the investment decisions once made cannot be reversed. The provisions of “Essential Commodities Act” are invoked from time to time to prevent free movement of goods from time to time. The policy of freight equalisation is a case in point. Providing subsidy to meet the transport cost of basic raw materials like coal and steel with a view to keeping the cost of production broadly uniform across the country. This not only caused burden of subsidy to be borne by the tax payer but also resulted in the allocation of resources not according to comparative advantage. Even though the policy has been given up, investment decisions once made can not be nullified without additional costs. Thus, even as the Centre made investment in the initial years after independence in major industrial projects in the resource rich poorer States, the latter could not reap the benefits of forward linkages. Not surprisingly, many steel based industries in other States like Punjab have become sick after the fright equalisation policy has been given up clamouring for subsidies and other tax concessions. In more recent years, with area based tax exemptions accorded to so called backward areas which includes the plains in Uttarakhand and Himachal Pradesh, the problem of migration of industries from the neighbouring States and resource distortions arising from them has become even more acute. These policies and regulations
have created several tariff zones within the country to alter resource allocation in unintended and inefficient ways.

Some of the State level policies ostensibly taken to protect the interest of the disadvantaged sections in urban areas, but has harmed their interest. The classic examples of these are the Rent Control Act and Urban Land Ceiling Act. Both policies have reduced investments in the housing sector and availability of rental housing at reasonable rents in urban areas for the potential migrants. Poor urban infrastructure, particularly water supply and sanitation facilities too are a major hindrance in the mobility of rural population to urban areas.

The basic impediment to mobility of people is the illiteracy, lack of skills, poor of information availability on employment situation and linguistic diversity. Linguistic diversity is a major impediment to mobility even within the four southern States, leave alone between the southern and northern States as there is no common language of communication. Illiteracy makes it difficult for the movement of labour from one place to another in search of livelihood and lack of skills makes the demand for such labour elastic with low productivity and wages. Given that the demand for such labour is mostly in rural areas, the mobility of labour from rural to urban areas is substantially reduced. Furthermore, the risks and lack of security for the rural unskilled labour in urban areas creates a lot of insecurity in the minds of potential migrants. In the event, the Harris – Todaro type of growth process can take place only in an imperfect manner, if it takes place at all.

(b) Accommodating Asymmetry:

As stated by Riker (1964) federalism is a bargain and every unit bargains and secures special advantages as a part of the agreement to join the federation. The extent of concessions it can get from the standard terms for joining the federation depends in its bargaining strength. While these are political arrangements and can strengthen or weaken the stability of the federation, they have significant implications on the way they impact on fiscal federalism. Therefore, it is useful to make a brief analysis of asymmetric federalism in India.

The independent India in 1947 began with a major asymmetry between British India and the princely States. In almost all cases, the princely States surrendered whatever notional

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14 For experiences of a number of federations in asymmetric federalism – developed and developing, see Bird (2007).
sovereignty they had to Independent India, in exchange for a guaranteed revenue stream: their “privy purses”. The nature of this bargain was clear: security and money in exchange for giving up authority or residual control rights. After independence, the Indian National Congress was in an extremely strong bargaining position, even relative to the coalition of the princes. Thus, even when there was no voluntary accession, such as Hyderabad, military force (the authority over which was also inherited from the British) ensured integration into the new Union.

While many of the former princely States (particularly the larger ones) continued as administrative units after their integration into India, this continuation was not an essential part of the bargain, and reorganisation of State boundaries from 1953 onwards, freely permitted to the Centre by the 1950 Constitution, gradually eroded this status. The Constitution allowed for sub-State structures for regions closely tied to some former princely States, but this had little practical import as the States became almost the sole significant sub-national units of governance. Thus, in general, the princely States ceased to matter as geographic entities. In this respect, the outcome was completely different from the standard case of a federation, where the constituents of the federation would normally retain their identities. Also, the asymmetries present in 1947 with respect to almost all the princely States disappeared from Indian federalism.

(i) Jammu and Kashmir

The major exception, of course, was the princely State of Jammu and Kashmir. While this State included several diverse populations and regions, the overwhelming majority of the population in the Kashmir valley was Muslim, and the State bordered the new nation of Pakistan. The history of the conflict over Kashmir has been written on extensively, even though there is no consensus on the interpretation of events in 1947-48. Here, it is merely noted that the State acceded to the Indian Union under very special terms, which were subsequently incorporated in the famous Article 370 of the Constitution. This article provided the State with a unique position in the Indian Union, with its own Constitution, a title interpreted as the equivalent of Prime Minister for its chief elected official, and a special assignment of functional responsibilities. Specifically, the jurisdiction of the Centre was restricted to foreign affairs, defence and communications, with the State’s legislature having residuary powers. The agreement reached in 1953, however, tried to incorporate the State into the mainstream and Centre’s powers were not limited to the three areas. This was in striking contrast to the situation of the other States,
where the Centre’s assignment of responsibilities was much more extensive, and where the Centre retained residuary powers. The recent act by the State Legislature of passing a resolution declaring autonomy to the State is an attempt to limit the powers of the Centre to defence, external affairs and macroeconomic policies.

While the political motivation and overtones are not the subject matter for discussion here, it is a matter to discuss afresh whether the assignment system and constitutional provision require a re-look and greater powers should be devolved to the States in administrative, political and fiscal matters. It is also important to examine the extent to which asymmetry in Union-State arrangements can be allowed. The matter has gained urgency in view of the recent demands for greater autonomy by Jammu and Kashmir.

(ii) The North-Eastern States

The process of administrative reorganisation of India in 1956 focused on the creation of new boundaries based on the main principle of language. Typically, separate religious, caste, ethnic or tribal identities within these boundaries were not the basis for further divisions. One major exception to this has been the Northeastern part of India, where there is a distinct difference in ethnicity from the rest of the country, and several strong divisions based not only on language, but also on culture and traditions. This part of India contains the States of Arunachal Pradesh, Assam, Manipur, Meghalaya, Mizoram, Nagaland, Sikkim and Tripura. Of these, only Assam has a population comparable to other typical Indian States. Most of these States were upgraded from the status of Union Territories\(^\text{15}\), this reclassification giving them, at one level, a political status equivalent to that of large States such as Uttar Pradesh and Bihar: for example, each State carries equal weight in mustering the fifty per cent of the States required to ratify an amendment to the Constitution.

However, the above eight States, along with Himachal Pradesh, Jammu and Kashmir and a more recent addition of Uttarakhand are “special category” States for the purpose of the allocation of financial resources by the Union government, and we revisit this issue later. Furthermore, there are several Constitutional provisions pertaining to the various Northeastern States. These involve various clauses of Article 371. These provisions have

\(^{15}\) At independence, of course, this entire region was administratively part of Assam province, and the union territories themselves were created by separation from Assam. Meghalaya was directly carved out of Assam State, while Sikkim was formerly an Indian protectorate.
been introduced through amendments, typically at the time of conversion of a Union territory into a State, or in the case of Sikkim, after its accession to India. They include language designed to protect or respect customary laws and religious practices, restrictions on the ownership and transfer of land, and restrictions on immigration. State legislatures are typically given final control over changes in these provisions.

It must be mentioned that there are various provisions in the Indian Constitution to protect group rights, and to compensate for initial inequalities in the social system. Thus the Constitution, while recognising the idea of fundamental human rights at the individual level, does not assume an idealised initial condition of equality, either in pure economic terms or otherwise. Thus there are allowances for separate laws to govern different religious groups, and there are provisions for various kinds of “affirmative action” for extremely disadvantaged groups. The first kind of provision simply respects diversity (though this can create issues of unequal treatment across subgroups, e.g., women in two different religious groups). The second attempts to correct for specific inequities, recognising that legislative equal treatment from very unequal initial conditions would not achieve desired equity goals. Conceptually, at this level of ethical or normative judgement, there is no difference between these provisions and the ones for the indigenous residents of Northeastern States, except that the latter happen to be geographically concentrated into reasonable administrative units.

However, in the perspective of federalism as a political and economic bargain, geography and demography matter in essential ways. Like in the case of Kashmir, the north-eastern States have enjoyed a relatively greater leverage than the States in general to enjoy a measure of asymmetric arrangement. In respect of these States, as in Kashmir, geographical concentration of ethnic (religious) groups, combined with a feeling of distinctness, has rendered the idea of political separation seem feasible, even though the economic rationale and feasibility of such separation may be questionable. This makes each of north-eastern States a significant bargaining unit, beyond what might be the case based on numbers alone. Put another way, a group with a similar size to that of the population of, say, Nagaland, just as distinctive, but scattered throughout the country, would not have the same bargaining position, in terms of obtaining special provisions in the Constitution. These factors have contributed to asymmetric arrangements in the Constitution.

(c) Institutional Weaknesses:

In a large and diverse fiscal federalism like India, there can be several sources of friction between the Centre and States and among the States *inter se*. In economic spheres there
can be several issues and frictions requiring resolutions arising from factors such as spillovers in public service delivery, mobility of people and resources, attempts to free ride by the Centre on the States through a variety of means including tax competition, tax exportation, passing of unfunded mandates, ownership issues relating to minerals and inter-State river water disputes. An important pre-requisite for efficient working of fiscal federalism is the evolution of a robust system of bargaining and that not only requires clearly laid down assignments and rules but also effective systems and robust institutions of bargaining and control.

Unfortunately, in the initial years of independence, intergovernmental bargaining and settlement were conducted in an environment of informality and such an arrangement sufficed at the time. During the Nehru era, which covered approximately the first decade and a half of the Constitution, the Prime Minister’s personal authority and prestige were combined with almost complete legislative control of the Centre and the States. Furthermore, Congress party was in power at both the Centre and in the States and the Prime Minister was able to settle all issues in an environment of informality. In such circumstances, issues of Centre-State relations were often played out within the ranks of the Congress party.

While general central political control in the Nehruvian era was expressed through the internal workings of the Congress Party, specific issues of Centre-State relations did emerge in more formal arenas. Issues of taxation and property rights related to particular provisions of the Constitution did involve explicit disputes between the Centre and the States that had to be adjudicated by the Supreme Court. One dispute related to clause (1) of Article 289, which exempts the property and income of the States from Central taxation. In 1951, the Centre attempted to bring business and trading operations of the States under the purview of acts governing customs duties and excise taxes. The States challenged this as an unconstitutional attempt to tax them. The judgement of the Supreme Court was a substantial victory for the Centre, reducing “the immunity of States from Union taxation to minuscule proportions” (Chanda, 1965, p. 89). The second dispute involved Article 294, which vested control of British Crown property in the pre-independence province of Bengal in the post-independence State of West Bengal. In 1957, the Centre enacted legislation claimed to be derived from an entry in the Union list, empowering

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16 One important example of substituting personal relations and party hierarchy for constitutionally mediated federal relations is the ‘Kamaraj Plan’ in the early 1960s in which all Central and State Ministers were made to resign except Nehru himself to enable the latter to exercise full discretion in governance.
Parliament to provide by law for “the regulation of mines and mineral development to the extent to which such regulation and development under the control of the Union is held to be expedient in the public interest.” The 1957 Act gave the Centre the power to prospect for coal in lands vested in the State of West Bengal. The State government took its case to the Supreme Court, which undertook an extensive and detailed review of the whole issue of federal relations, subnational sovereignty and divisions of powers, including the evolution of the Constitution. Once again, the final judgement was in favour of the Centre’s position and power. While both cases involved some dissent, ultimately the basic centralising bias of the Constitution can be viewed as having tilted the interpretation of the court against the States in both cases.

A critical element in promoting co-operative federalism” is the mechanism and institutional structure for bargaining. Bargaining is easier when all the parties involved stand to gain, but becomes difficult when one party’s gain is necessarily at the cost of the other. In any case, existence of institutions to negotiate and resolve issues is critical. The Sarkaria Commission went into this question and recommended the appointment of the Inter-State Council. Although much was expected of the Inter-State Council appointed in 1990 in improving the protocols for bargaining to achieve co-operative solutions in the strategic game between the Centre and States and among the States inter-se, unfortunately, in practice the Inter-State Council has been ineffectual by the very nature of its constitution. Besides the lack of power and stature, the Inter-State council constituted under the Union Home Ministry will not be perceived as an impartial negotiator or arbiter by the States.

Another institution that was created to facilitate and coordinate the planning process in the country is the National Development Council (NDC). The Council is chaired by the Prime Minister and the members include the cabinet Ministers of the Centre, State Chief Ministers and the deputy Chairman and members of the Planning Commission. One can view this as an institution not only to foster both vertical and horizontal cooperation but also to resolve all outstanding issues between the Centre and States and among the States inter se. Unfortunately, the NDC has not evolved itself into taking such a role. The meetings of NDC are far too infrequent to undertake the above task and the meetings are a mere ritual in which the each Chief Minister gives a speech without any follow up action.

In a democratic polity, the Parliament remains the primary forum for raising concerns about Centre-State issues. Surely, the Rajya Sabha, the Council of States should safeguard

17 See Chanda, Section 3.4 for a detailed discussion of the court’s arguments.
the States’ interest. In countries like the United States, the Senate has been playing a constructive role in safeguarding the interest of the States. However, when the choice of the candidates to be nominated to the Rajya Sabha by every political party based on the political considerations rather than representing the States they are nominated from, the institution fails to safeguard the interest of the States.

In this context, it is important to refer to the new institutional arrangement to harmonise the sales tax system that has emerged for calibrating reforms in the sales tax system in the country. In the aftermath of the Report on Domestic Trade Taxes submitted to the Union Finance Ministry by the National Institute of Public Finance and Policy (NIPFP, 1994) in 1994, the Committee of the Finance Ministers which eventually became the Empowered Committee of State Finance Ministers embarked upon the process of reforming the State level consumption taxes. The Committee has been an important catalyst in evolving consensus for harmonising sales tax systems in different States and has worked as an effective forum to project a united front in negotiating with the Centre in calibrating reforms. This is an important example of how institution of bargaining and negotiation can be effective when there are mutual gains to be had. Nevertheless, the forum is an ad hoc arrangement; it does not have any statutory standing and it is difficult to see it can evolve itself as an institution for bargaining and negotiation between the Centre and the States and among the States inter-se.

In spite of these ad hoc arrangements to deal with specific cases, there are many instances where the need for an institutional mechanism for negotiation and bargaining has been felt. In fact, prevailing institutions are inadequate to address the issues of not merely the cases where the bargaining could result in mutual gains. There are perennial issues relating to both between the Centre and States and between one State and another requiring a permanent secretariat and resolution. These could relate to sharing of river water, claims to royalty from minerals, encroachment of States’ domain by the Centre and vice versa, matters pertaining to area under concurrent jurisdictions or design and implementation issues relating to the design and implementation of any of the umpteen central sector and centrally sponsored schemes. Even in the case of the introduction of VAT or GST, there is a need for an institution to monitor the commonly agreed principles and rules on a continuous basis.

(d) Sharing of Water Resources \(^{18}\)

(i) Overlapping domains and settlement procedure

Inadequacy of institutional system is nowhere as glaring as in the case of water dispute

\(^{18}\) This part has been taken from the joint work with Nirvikar Singh (Rao and Singh, 2005).
settlement. While the nature of the dispute and its emotional appeal to the population in all the States where the water flows can be a major factor, institutional vacuum is equally an important reason for the inability of the parties to resolve the dispute. Indeed, this is an area where Coasian bargains should work; but the experience also demonstrates the failure of the Coasian bargaining in resolving the disputes. It is therefore, necessary to analyse the entire issue of sharing of water resources in some detail.

Indeed, the issue of water sharing is one of the most important issues in Indian federation. It is therefore not surprising that the Commission on Centre-State Relations (India, 1988) devoted an entire chapter on the subject and made a series of recommendations. The provisions of the Indian Constitution dealing with the inter-State river water disputes are:

- Entry 17 in the State List,
- Entry 56 in the Union List, and Article 262.

The first provision makes water a State subject, but qualified by Entry 56 in the Union List, which States: “Regulation and development of inter-State rivers and river valleys to the extent to which such regulation and development under the control of the Union is declared by parliament by law to be expedient in the public interest.” Article 262 explicitly grants parliament the right to legislate over the matters in Entry 56, and also gives it primacy over the Supreme Court. As documented by Iyer (1994), Parliament has not made much use of Entry 56. Various River Authorities have been proposed, but not legislated or established as bodies vested with powers of management. Instead, river boards with only advisory powers have been created.

Hence, State governments dominate the allocation of river waters. Since rivers cross State boundaries, disputes are inevitable in this institutional setting. The Inter-State Water Disputes Act of 1956 (ISWD) was legislated to deal with conflicts, and included provisions for the establishment of tribunals to adjudicate where direct negotiations have failed. However, States have sometimes refused to accept the decisions of tribunals. Therefore, arbitration is not binding. Significantly, the courts have also been ignored on occasion. Finally, the Centre has sometimes intervened directly as well, but in the most intractable cases, such as the sharing of the Ravi-Beas waters among Haryana, Jammu and Kashmir, Rajasthan, and Punjab, central intervention, too, has been unsuccessful. An unambiguous institutional mechanism for settling inter-State water disputes does not exist.
As is the case with several other aspects of modern India’s laws and institutions, water institutions have their origins in pre-independence legislation. The Government of India (GOI) Act 1919, made irrigation a provincial subject, while matters of inter-provincial concern or affecting the relations of a province with any other territory were subject to legislation by the central legislature. The GOI Act of 1935 drew attention explicitly to river disputes between one province and another or between a province in British India and a (federated) Indian State. The provincial legislative list (which became Entry 17 in the State List in the 1950 Constitution) included water, that is to say water supplies, irrigation and canals, drainage and embankments, water storage and water power. Sections 130 to 134 in the 1935 Act dealt with the problem of interference with water supplies. The provisions laid down that a province or a princely State could complain to the Governor General if its interests were prejudicially affected in the water supplies from a natural source, due to the action of other province or princely State. The Governor General could appoint a commission to investigate the matter and after considering its report could give his decision. The decision was binding on all the parties concerned.

In the Constitution of India Articles 239 to 242 were worded on the same lines as sections 130 to 134 of the 1935 Act. Subsequently, these were replaced by Article 262. The Provisions of Article 262 reads:

1) Parliament may by law provide for the adjudication of any dispute or complaint with respect to the use, distribution and control of the waters of, or in any inter-State rivers or river valleys.

2) Notwithstanding anything contained in this Constitution, Parliament may, by law, provide that neither the Supreme Court nor any other Court shall exercise jurisdiction in respect of any such dispute or complaint as is referred to in Clause (1) “.

Within the powers available under Entry 56 of the Union List and Article 262, Parliament enacted two laws. The first was the River Boards Act of 1956, which enabled the setting up of river boards to ensure optimum utilization of water resources of inter-State rivers and promote schemes for irrigation, water supply, drainage, development of hydroelectric power and flood control. The second, Inter-State Water Disputes Act, 1956 provided for Central Government referring the disputes relating to the use, distribution, or control of Inter-State river waters for adjudication to a tribunal constituted under the Act at the request of the affected State.

The tribunal is required to investigate the complaint and make an award. Within three months of the report, the Central Government or any of the State government concerned
can approach the tribunal for clarification. The Central Government shall publish the tribunal's decision in the official gazette. The decision will be final and binding on the parties to the dispute. Neither the Supreme Court nor any other court can exercise jurisdiction in respect of any water dispute referred to a tribunal.

(ii) Experience of Resolving Water Disputes

Indian water laws, give an appearance of clarity and certainty. However, actual experience of solving disputes has had considerable opaqueness and indeterminacy. The law permits considerable discretion, and different disputes have followed quite different paths to settlement, or in a few cases, continued disagreement.

The Central Government has had to give substantial attention to water disputes which began to emerge soon after the framing of the Constitution. As far back as 1967, 15 cases were identified. Of this seven disputes have been resolved through mutual discussions and negotiations. Of the remaining eight, the Krishna-Godavari Water Dispute, Cauvery Water Dispute and Narmada Water Dispute are major disputes involving large river basins. These were referred to tribunals with varying degrees of success. The Tribunal on Cauvery Water Dispute is still functioning and is yet to make a final award. The interim award of the tribunal was strongly contested by Karnataka which also went to the extent of boycotting the tribunal. The remaining five disputes are of minor nature and possibly could perhaps be resolved through negotiations.

An important issue that should be noted in the context of conflict resolution with regard to the water disputes is that although under Article 262 of the Constitution, Inter-State Water Disputes Act has been passed, the Centre has failed to use the broader powers under Entry 56 (Iyer, 1994). Some have opined that this was a deliberate act by the Union government to keep the conflicts alive because, it allows discretion in bargaining for the Union over States relations in general by keeping the contradiction between the States alive.

Another striking case of inaction, which illustrates several of the above problems, is the Ravi-Beas dispute between Punjab and Haryana. In fact, the river water dispute has led to a serious confrontation between the Centre and some groups in Punjab. Difficulties may partly be due to incomplete information. In particular, as initial rights are not defined with respect to the quantity of water beyond historic usage, the situation is one of conflict over property rights and this has hindered agreement. Uncertainty over the future political
situation has also mattered, with different parties at different times waiting for more favourable bargaining situations rather than reaching agreement.

Analysis shows that there is an urgent need for examination of the institutions that have been created since 1980. The central ministry of irrigation published a document in 1980 outlining a proposed study of India’s national water resources. This led to the formation of the National Water Development Agency (NWDA) in July 1982, to “carry out the water balance and other studies...for optimum utilization of water resources...”. This is a Government of India agency in the Ministry of Water Resources, and not a body with any statutory backing. Furthermore, its scope is technical, and separate from the institutional realities of water allocation. In 1983, the National Water Resources Council (NWRC) was created by a Central Government resolution. Its composition includes Chief Ministers of States, Lieutenant Governors of Union Territories, several Central Government ministers, and the Prime Minister is the Chairman. This group first met in October 1985, and adopted a National Water Policy in 1987. This policy emphasizes an integrated and environmentally sound basis for developing national water resources, but provides no specific recommendations for institutions to achieve this. Though the council was created out of disenchantment with the adjudicatory process for inter-State river disputes, it has not provided concrete proposals to improve that process, nor has it provided the useful alternative that was hoped for, as indicated by the persistence of the Ravi-Beas and Cauvery disputes. This, however, should not be a surprise for, the NWRC does not meet any of the required: it does not provide specific mechanisms for dispute resolution, it does not delegate sideways to achieve commitment possibilities, and it does not have any statutory force. While it may provide a useful forum for long range planning and information exchange, its usefulness otherwise has been limited. Thus, despite establishing NWDA and NWRC, the mechanism to resolve disputes has remained ineffective.

The final issue that deserves discussion is the enforcement of tribunal awards. This issue was given some attention by the Sarkaria Commission. It noted that Section 6 of the ISWD Act of 1956 provides that the Union Government shall publish the decision of the Tribunal in the Official Gazette and the decision shall be final and binding on the parties to the dispute and shall be given effect by them. The Commission’s report goes on to suggest that the Centre cannot enforce the tribunal award if a State government refuses to implement it. It notes that the amendment of the Act in 1980, inserting Section 6A, which provides for an agency to implement a tribunal award, is not sufficient because such an agency cannot function without the cooperation of the States concerned. The
Sarkaria Commission’s recommendation is, therefore, that a water tribunal’s award should have the same force and sanction behind it as an order or decree of the Supreme Court.

This has not been done, but it should be noted that water tribunals already have such court-equivalent powers for a narrow range of issues, including gathering of information, requiring witnesses to testify and recovering the costs of the tribunal. Furthermore, the ISWD Act, Section 11 States that, “Notwithstanding anything contained in any other law, neither the Supreme Court nor any other court shall have or exercise jurisdiction in respect of any water dispute which may be referred to a Tribunal under this Act”.

Although this provision gives water tribunals broadly an equivalent status to the Supreme Court, it would be extremely difficult to enforce the decision if the State decides not to accept it! Thus, the resolution of water disputes is complicated by being tangled in the general difficulties of Centre-State federal issues and it is doubtful whether amendment of the Act itself will solve the problem.

The Sarkaria Commission’s other recommendations were based on the same kinds of difficulties in resolving past disputes as have been described in this paper. Two recommendations related to placing time limits on constituting tribunals and having them to deliver the decisions. These merely echoed the recommendations of the Administrative Reforms Commission (India, 1968). Another recommendation was that the Centre could appoint a tribunal without being asked to do so by a State government. A final recommendation was for the establishment of a national level data bank and information system. None of these recommendations has been implemented. It must be suggested that the failure to secure satisfactory resolution of water dispute partly reflects the fundamental nature of the problem, that water issues are tangled with broader difficulties in the federal structure. The solution, in addition to the above recommendations, must include the creation of a quasi-independent hierarchy of institutions to manage the allocation of water. This will insulate the process from political uncertainties, and permit a greater degree of commitment and cooperation. The central point to be emphasized is that appropriate institutions can play a vital role in shaping and constraining the incentives of the actors in inter-State water allocation.

(iii) Dispute settlement procedures:

Constitutionally and legislatively, inter-State river dispute settlement procedures involve either of two processes: negotiations and compulsory legal adjudication. Furthermore,
there is room for voluntary processes such as mediation, conciliation and voluntary arbitration, often by the Prime Minister or other members of the Central Government. Such processes do not foreclose arbitration or adjudication on specific areas of conflicts which remain unresolved after mediation and conciliation. Guhan (1993) suggests that mediation and conciliation do not have enough scope in resolving water disputes, and that “adjudication inevitably leads to adversarial positions and maximal claims”. Iyer (1994) points out that this criticism of adjudication misses the point, since the difficulty of reaching an agreement may be structural, and assisted negotiations (that is, conciliation and mediation by a third party) may be as problematic as unassisted negotiations. He emphasizes the importance of goodwill, and willingness to accept an “objective settlement”, but does not really come to grips with the structural issues.

A key insight of our discussion is that the processes and institutions as they currently exist for resolving inter-State river disputes are not well-defined or definite. There are too many options, and too much discretion and too many stages of the process. As the utilization of water increases, the possibility of disputes multiply, and it is necessary that the dispute resolution mechanism should be better defined. Despite definitiveness in the award of the tribunals in letter, they too have not been effective. Thus, the entire conflict resolution in the case of water disputes has remained an open issue.

The problem has been compounded by inordinate delays. Firstly, there has been extreme delay in constituting tribunals. Under Section 4 of the ISWD Act, the Union government is required to set up a tribunal only when it is satisfied that the dispute cannot be settled by negotiations. The Centre can thus indefinitely withhold the decision to set up a tribunal on the ground that it is not yet satisfied that negotiations have failed.

Secondly, tribunals have taken long periods of time to give their awards. This can be traced to two factors: first, the time taken for assembling facts and hearing arguments and second, abortive attempts to bring about solutions at a political level, which delayed the functioning of tribunals. It took nine years from reference in the case of the Narmada Tribunal, four years in the case of the Krishna Tribunal and ten years in the case of the Godavari Tribunal. Finally, there have been delays in notifying the orders of tribunals in the Government of India’s official gazette; this has resulted in delays and uncertainty in enforcement. The process took three years in the case of the Krishna Award and one year in the case of the Godavari Award. These delays naturally tend to complicate the dispute settlement process.
The kinds of recommendations with respect to delays are old ones, going back to the Administrative Reforms Commission report of 1969, and repeated by the Sarkaria Commission in 1988. To reduce delays, the Centre as well as any State that is involved in a dispute should be able to request adjudication. The process of adjudication should begin within a prescribed time (for example, six months or one year) and conclude within a prescribed time (for example, three or five years).

(iv) Enforcement

A major issue relating to water dispute is the enforcement of the award of the tribunals. State governments have sometimes rejected tribunal awards, as in the case of Ravi-Beas Tribunal and the Punjab government. In this case, the Central Government avoided notifying the tribunal’s award to prevent further deterioration of the disturbing political situation in Punjab. In the case of the Cauvery dispute, the tribunal’s interim order was sought to be nullified by the Karnataka government through an ordinance. Though the Supreme Court pronounced that the ordinance was unconstitutional, the Karnataka government showed no inclination to implement the tribunal’s interim order, until a compromise was reached through political negotiations behind closed doors. The Sarkaria Commission was of the view that in order to make tribunal awards binding and effectively enforceable, the ISWD Act should be amended to give these awards the same sanction as an order or decree of the Supreme Court.
Functioning of Indian Fiscal Federalism

As discussed earlier in the paper, the Constitution demarcates revenue and expenditure powers of the Union and State governments and the latter have to share powers with local governments as indicated in separate schedules for the urban and rural areas. The Constitution recognises that there is inherent imbalance in the assignment of revenues and expenditures between the Centre and States and among the States inter se and provides for an impartial, semi-judicial body – the Finance Commission to be appointed every five years or earlier to review the finances of the Centre and States and make recommendations of the resources to be transferred to the States from the Centre to enable them to provide the services in their domain in a satisfactory manner. In addition, with the adoption of planned development strategy, the Planning Commission also started transferring resources from the Centre to the States by way of grants and loans based on the formula determined by the National Development Council 19 and different central ministries give specific purpose transfers to States.

The local governments below the States number over a quarter million with about 3000 in urban areas and the remaining, rural. The urban local governments consist of municipal corporations in large cities, municipalities in smaller cities and town Panchayats and notified areas in smaller towns. Rural local governments are at district, Taluk (block) and village levels. Each State has devolved powers to levy certain taxes and fees to the village panchayats and urban local bodies. The States have also instituted a system of sharing of States’ revenues and giving grants to urban and rural local bodies. Each State is required to appoint a State Finance Commission to review the finances of the local bodies and assign tax shares and make grants every five years. The local governments are also entrusted with the task of implementing several Central schemes.

a. The Assignment Question

(i) Assignment between Centre and States

The tax and expenditure powers of the Central and the State governments are specified in the seventh schedule to the Constitution. The functions required for maintaining macroeconomic stability, international relations and activities having significant scale economies have been assigned placed in the Union or the Concurrent List. The functions

19 This is called the ‘Gadgil’ formula after the name of the Deputy Chairman of the Planning Commission (Prof. D. R. Gadgil) who announced the formula for the first time in 1969.
which have a State-wide benefit zone are assigned to the States. Most broad-based and progressive taxes have been assigned to the Centre. The Centre also has residual tax powers. A number of tax handles have been assigned to the States as well, but from the viewpoint of revenue productivity, only the sales tax is important. The States can borrow from the Central Government. They have the powers to borrow from the market as well, but if a State is indebted to the Central Government, the borrowing must be approved by the Centre.

Tax powers are assigned according to the principle of separation, exclusively either to the Centre or to the States. However, exclusivity is not so easily defined and a number of anomalous situations have emerged. Thus, the Centre can levy taxes on production (excise duty) but the tax on the sale of goods is leviable by the States. Similarly, taxes on agricultural incomes and wealth are in the States’ domain whereas those on non-agricultural incomes and wealth are a Central prerogative. The States find taxing agricultural incomes politically infeasible and administratively difficult. This has provided a way to evade the income tax levied by the Centre.

The Constitution recognises that the States’ tax powers are inadequate to meet their expenditure needs and therefore, provides for the sharing of revenues from central taxes. Prior to the enactment of the Constitution (Eightieth Amendment) Act 2000, taxes on incomes other than non-agricultural incomes and union excise duty were shared with the States. Considering the potential adverse incentives of sharing of taxes from individual sources for the Central Government, based on the recommendations of the Tenth Finance Commission, the Constitution was amended to include proceeds from all central taxes in the divisible pool. In addition to tax devolution, the Constitution provides for making grants in aid to the States (Article 275). Both tax devolution and grants in aid must be determined by the Finance Commission, an independent body appointed by the President every five years (Article 280).

The shares of Central and State governments in revenues and expenditures are summarised in Tables 1 and 2. The States, on an average, raise about 34 per cent of revenues and incur 58 per cent of expenditures. However, the States’ autonomy in implementing expenditures is less than what is suggested by these figures as they are required to make matching contribution to central schemes. The States’ expenditures on these schemes increased from 7 per cent of the total in 1985-86 to about 20 per cent in 2000-01. However, since 2003-04, the Central Government has been transferring funds directly to implementing agencies which were earlier routed through the State budgets.

The pattern of expenditures shown in Table 2 indicates that the Central Government plays a major role in defence and in the provision of large physical infrastructure facilities.
On the other hand, the States have a high share of total government expenditures on internal security, law and order, and social services, and economic services like agriculture, animal husbandry, forestry, fisheries, irrigation and power and public works. The States’ share in expenditure on administrative services is about 68 per cent; on social services they spend about 80 per cent and on economic services their share is over 60 per cent. Their role in providing social services like education, public health and family is over 80 per cent.

<table>
<thead>
<tr>
<th>Sr. No.</th>
<th>Tax</th>
<th>Per cent of GDP</th>
<th>Per cent of Total Tax Revenue</th>
</tr>
</thead>
<tbody>
<tr>
<td>I</td>
<td>Central Taxes</td>
<td></td>
<td></td>
</tr>
<tr>
<td>I.1</td>
<td>Personal Income tax</td>
<td>2.5</td>
<td>11.3</td>
</tr>
<tr>
<td>I.2</td>
<td>Corporation Income tax</td>
<td>4.1</td>
<td>18.3</td>
</tr>
<tr>
<td>I.3</td>
<td>Central excise duties</td>
<td>2.6</td>
<td>11.8</td>
</tr>
<tr>
<td>I.4</td>
<td>Service Tax</td>
<td>1.1</td>
<td>4.9</td>
</tr>
<tr>
<td>I.5</td>
<td>Customs duty</td>
<td>2.2</td>
<td>9.9</td>
</tr>
<tr>
<td>I.6</td>
<td>Other taxes</td>
<td>0.1</td>
<td>0.2</td>
</tr>
<tr>
<td></td>
<td><strong>Total – Central Taxes (Gross)</strong></td>
<td>11.6</td>
<td>56.4</td>
</tr>
<tr>
<td></td>
<td><strong>Total – Central Taxes (Net)</strong></td>
<td>9.4</td>
<td>41.8</td>
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<tr>
<td></td>
<td><strong>Total Central revenues (Gross)</strong></td>
<td>14.8</td>
<td>66.1</td>
</tr>
<tr>
<td></td>
<td><strong>Total – Central Revenues (Net)</strong></td>
<td>11.6</td>
<td>51.5</td>
</tr>
<tr>
<td>II</td>
<td>State taxes</td>
<td></td>
<td></td>
</tr>
<tr>
<td>II.1</td>
<td>Tax on incomes</td>
<td>0.1</td>
<td></td>
</tr>
<tr>
<td>II.2</td>
<td>Taxes on transfer of Property</td>
<td>0.9</td>
<td></td>
</tr>
<tr>
<td>II.3</td>
<td>Sales taxState excise duties</td>
<td>4.0</td>
<td></td>
</tr>
<tr>
<td>II.4</td>
<td>Taxes on transport</td>
<td>0.7</td>
<td></td>
</tr>
<tr>
<td>II.5</td>
<td>Others</td>
<td>0.5</td>
<td></td>
</tr>
<tr>
<td>II.6</td>
<td>Total – State taxes (Own)</td>
<td>0.3</td>
<td></td>
</tr>
<tr>
<td>II.7</td>
<td>Total – States’ Own Revenues</td>
<td>6.4</td>
<td>27.9</td>
</tr>
<tr>
<td>II.8</td>
<td>Total – State taxes (Accrual)</td>
<td>7.5</td>
<td>33.9</td>
</tr>
<tr>
<td></td>
<td><strong>Total – States, Revenue (Accrual)</strong></td>
<td>9.4</td>
<td>42.0</td>
</tr>
<tr>
<td></td>
<td><strong>Total taxes</strong></td>
<td>13.4</td>
<td>59.8</td>
</tr>
<tr>
<td></td>
<td><strong>Total revenues</strong></td>
<td>18.922.4</td>
<td>84.3100.0</td>
</tr>
</tbody>
</table>

* Revised Estimates. ** Netted for the interest paid to the Central Government.

**Source:** Public Finance Statistics, Ministry of Finance, Government of India, 2007-08.
(ii) **Assignment between State and local governments:**

With the Constitutional Amendments in 1992, roles and responsibilities of rural and urban local governments have been specified. Accordingly, in separate schedules, a list of 29 functions to rural local bodies and another list of 18 functions to urban local bodies have been specified. However, the revenue and expenditure assignments in the lists are concurrent with the States’ responsibilities and the actual assignment of specific revenue sources and expenditure depends on the extent to which the State is willing to devolve. However, the extent of devolution of powers and functions to local governments shows wide variation among the States.

**Table 2**

<table>
<thead>
<tr>
<th>Sharer of State Governments in Total Expenditure</th>
<th>2000-01</th>
<th>2006-07</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Revenue</td>
<td>Capital</td>
</tr>
<tr>
<td><strong>I. Non-Developmental Expenditure</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>A. Interest Payment</td>
<td>41.0</td>
<td>0.0</td>
</tr>
<tr>
<td>C. Administrative Service</td>
<td>63.7</td>
<td>62.9</td>
</tr>
<tr>
<td><strong>II. Development Expenditure</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>E. Soc. and Com. Services</td>
<td>82.2</td>
<td>80.8</td>
</tr>
<tr>
<td>i. Education</td>
<td>89.4</td>
<td>67.4</td>
</tr>
<tr>
<td>ii. Medical and Health</td>
<td>86.7</td>
<td>98.6</td>
</tr>
<tr>
<td>iii. Family Welfare</td>
<td>76.2</td>
<td>100.0</td>
</tr>
<tr>
<td>iv. Others</td>
<td>57.1</td>
<td>55.5</td>
</tr>
<tr>
<td>F. Eco. Services, of which</td>
<td>57.4</td>
<td>71.3</td>
</tr>
<tr>
<td>i. Agriculture etc.,</td>
<td>64.0</td>
<td>98.4</td>
</tr>
<tr>
<td>ii. Industry and Minerals</td>
<td>40.4</td>
<td>50.3</td>
</tr>
<tr>
<td>iii. Power, Irrig. Flood Control</td>
<td>90.3</td>
<td>85.4</td>
</tr>
<tr>
<td>iv. Tpt. and Communication</td>
<td>37.7</td>
<td>69.4</td>
</tr>
<tr>
<td>v. Others</td>
<td>30.3</td>
<td>27.9</td>
</tr>
<tr>
<td>H. Loans and Advances</td>
<td>0.0</td>
<td>26.1</td>
</tr>
<tr>
<td>I. Total</td>
<td>56.0</td>
<td>58.4</td>
</tr>
</tbody>
</table>

**Source:** Indian Public Finance Statistics, Ministry of Finance, Government of India.
The problem with the devolution is the lack of clarity in the roles of the local governments, in both urban and rural areas. Besides overlapping jurisdiction with the State governments the local governments have to contend with the encroachment of their legitimate roles by various service providers and user groups. Overlapping jurisdictions impacts adversely on service delivery, it results in loss of accountability and results in the higher level governments pushing unfunded mandates on lower level governments. In the case of rural local bodies, there has been an attempt to undertake activity mapping, but that has not gone far in clarifying the assignment system.

In addition to the transfers recommended by the State Finance Commissions, the local governments receive funds for the implementation of various central schemes. The most important is for poverty alleviation, but there are also other schemes for social and community services in which the local governments have a comparative advantage in implementation. Even apart from conditional grants, local governments have very little flexibility in the use of funds (Rao, Amar Nath and Vani, 2003). After deductions of charges for electricity and other facilities by State government, very little is left in the general purpose transfers. In general, there are few funds available to execute developmental schemes.

In spite of the fact that the Constitution has tried to bring in clarity in the assignments, there are substantial overlapping in the systems. As discussed earlier, over the years, there were encroachments into States’ domain by the Centre for various reasons, including the implementation of centralised planning process. While the system has managed to stretch to accommodate the requirements, there has been a significant cost in terms of lack of economy, accountability and efficiency in public service delivery. It is, therefore, important to review the system of assignments to ensure clarity and harmony in revenue and expenditure decisions.

As regards the assignment of taxes are concerned, the adoption of the principle of separation is an attempt to bring in clarity. However, given the interdependence of tax bases separation can not be done in the economic sense and not surprisingly, the arrangement has not helped to develop the tax system on scientific lines and has created substantial overlap in the tax systems of the Centre and States. The exemption of agricultural income tax has prevented taking the comprehensive concept of income as the base for taxation and this has opened up avenues for large scale evasion and avoidance of taxes. This has also brought in a sense of inequity in the horizontal equity sense. In the case of consumption taxes the arrangement has entailed large scale overlapping of the tax system. The Centre is allowed to levy excise duties on manufactured goods and
the tax on the sale or purchase of goods is assigned to the States and both are taxes on consumption. Whereas the excise duty on manufacturing product is a levy at the first point of sale the sales tax is a levy that can be levied at any or all the sale points. In other words, both the taxes fall on the same base and in a system where there is no harmonisation, this has led to the evolution of non-transparent consumption tax system. Thus, the attempt to separate the tax powers of the Centre and States in the Constitutional assignment has not helped the governments to develop the tax systems which are comprehensive and harmonious. In contrast, in countries like the United States and Canada, both income taxes and taxes on consumption are levied concurrently by the Centre and States and in the United States, even by local governments. Yet, these countries have been able to work out a much more harmonised system, often with the Centre determining the base and the States and local governments piggybacking their own rates on this base.

Development of the tax system on modern lines calls for a paradigm shift in tax assignments. It is necessary to recognise that Central and State tax bases are interdependent and enable concurrent tax powers to Centre and States in respect of both income and domestic consumption taxes. In the case of personal income tax, as mentioned above, separation of tax powers between the Centre and States based on whether the income is from agricultural or non-agricultural sector has been a major source of tax evasion. As agriculture is transformed into a business it is important to levy the tax on incomes received from all the sources both for reasons of neutrality and to minimise tax evasion. At the same time, the Centre, States and even the major metropolitan cities could be allowed to levy the tax with both the States and the cities allowed to piggyback their levies on the tax base determined by the Centre and subject to ceiling rates. This will empower both the States and the metropolitan cities with own revenue handles and provide the much needed resources to provide State level public services as well as civic amenities and avoid resorting to inefficient taxes like Octroi. On the indirect taxes front, the attempt to levy the Goods and Services Tax (GST) by the Centre and States will go a long way in harmonising the consumption tax system. Harmonising the tax system on the lines indicated above is important in a globalising environment not only to develop a tax system which minimises distortions and compliance costs but also to provide sufficient resource handles to the subnational governments to provide efficient levels of public services assigned to them.

(b) Fiscal Imbalances: Trends and Issues

(i) Vertical Fiscal Imbalance in India:

Constitutional assignments and developments over the years have contrived to create a
high degree of fiscal centralisation and vertical fiscal imbalance. This is described in Table 3. As mentioned earlier, in 2008-09, the States raised about 34 per cent of total revenues and incur 58 per cent of States’ total expenditures. Their own revenues financed 61 per cent of their revenue expenditures and about a half of their total expenditures in 2008-09. The States’ own revenues in the total have shown a marginal increase from about 35 per cent until 1990-91 to about 38 per cent in 2006-07, but declined to 34 per cent in 2008-09. However, their share in expenditures has increased at a much sharper rate from about 51.7 per cent in 1990-91 to 58.4 per cent in 2006-07. However, this does not signify an increase in decentralization for (i) fiscal dependence of the states on central transfers has shown an increasing trend and (ii) increasing proportion of State spending is financed from specific purpose transfers on which the States’ have little manoeuvrability have shown a sharp increase in recent years. In fact, in respect of a number of schemes, since 2003-04, Central assistance is given directly to the implementing agencies bypassing the state budgets. Thus, inter-temporal comparison gets vitiated as since 2003-04, both the States’ expenditure on these schemes and the transfers received from them are not included in the state budgets.

Table 3

<table>
<thead>
<tr>
<th>Year</th>
<th>Per cent of States’ own current revenues total current revenues</th>
<th>Per cent of States’ current expenditure to total current expenditure</th>
<th>Per cent of States’ own current revenues to States’ current Expenditure</th>
<th>Per cent of States’ expenditure* to total expenditure*</th>
</tr>
</thead>
<tbody>
<tr>
<td>1960-61</td>
<td>36.6</td>
<td>59.9</td>
<td>63.9</td>
<td>56.8</td>
</tr>
<tr>
<td>1970-71</td>
<td>35.5</td>
<td>60.2</td>
<td>60.6</td>
<td>53.9</td>
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<tr>
<td>1980-81</td>
<td>35.6</td>
<td>59.6</td>
<td>60.1</td>
<td>56.0</td>
</tr>
<tr>
<td>1990-91</td>
<td>35.2</td>
<td>54.6</td>
<td>53.1</td>
<td>51.7</td>
</tr>
<tr>
<td>2000-01</td>
<td>37.8</td>
<td>56.0</td>
<td>48.6</td>
<td>56.1</td>
</tr>
<tr>
<td>2005-06</td>
<td>38.1</td>
<td>55.2</td>
<td>60.9</td>
<td>56.2</td>
</tr>
<tr>
<td>2006-07 (RE)</td>
<td>38.0</td>
<td>57.0</td>
<td>60.7</td>
<td>58.4</td>
</tr>
</tbody>
</table>


Although intuitively, it looks simple, there are formidable conceptual and measurement difficulties in operationalising both centralisation and fiscal balance. See, Bird (1986).
(ii) Horizontal Fiscal Imbalance

An important feature of Indian fiscal federalism is the wide inter-State differences in revenue capacity and consequently, per capita expenditures. There are 17 relatively more homogenous general category States, but even these have wide differences in size, revenue raising capacities, efforts, expenditure levels and fiscal dependence on the Centre. In addition, in terms of economic characteristics the 11 mountainous States of the north and the Northeast differ markedly from the rest and therefore are considered ‘special category’ States. Of the 28, three additional States of Chattisgarh, Jharkhand and Uttarakhand were created 2001 after the bifurcation of Madhya Pradesh, Bihar and Uttar Pradesh respectively.

The selected fiscal indicators of the States shown in Table 4 bring out several important features. First, there are wide inter-State variations in revenues in both per capita terms and as a per cent of Gross State Domestic Product (GSDP). Second, these variations indicate differences both in revenue capacity and in revenue effort. Third, the tax-GSDP ratios in the special category States are lower than in the general category States, even when their per capita GSDP is higher. This is partly because, in these States there is not much production activity and government administration is the major determinant of the GSDP. Fourth, although the revenue bases in the special category States are low, their average per capita development expenditures are higher than not only the all-State average but also higher than the average of high income States. Fifth, in the case of general category States, the fiscal dependence on the Centre is not only high but also varies inversely with per capita income. Per capita development expenditures in high income States was higher than the all-State average by 44 per cent and that of the low income States is lower by 36 per cent. Nevertheless, there has been significant equalisation; while the per capita revenues from own sources in low income States were about 29 per cent of those in high income States, per capita expenditure in the former was close to 63 per cent.

The inter-State disparities among the general category States are not only high, but have shown an increasing trend. In 1980-81, the per capita SDP in the richest State, Punjab (Rs 2674) was about 2.9 times that of the poorest, Bihar (Rs 919). In 2006-07, this difference increased to 4.8 times with per capita SDPs of Haryana, the highest income State at Rs. 48214 and Bihar at Rs. 10286 (Table 4). It is also seen that per capita income

\[21\] Of course, the higher than average per capita expenditures in special category States cannot be entirely attributed to their inherent cost disability. This may also be due to poor fiscal management.
levels have tended to diverge sharply after market based reforms were initiated. (Rao, Shand and Kalirajan, 1999). With economic liberalization, the States with better access to factor and product markets and better transport infrastructure and connectivity were able to take greater advantage of the opportunities as compared to those with poor transport infrastructure and low levels of market development.

As inter-State differences in the ability to raise revenues have increased over the years, and as federal transfers did not entirely offset the fiscal disabilities of the poorer States, the coefficient of variation in expenditures also increased over the time period (Rao, 1998). A detailed analysis of the pattern of regional development in India shows that the poorer States are the ones with abundant natural resources including minerals. While the benefits of the rich mineral resources accrue to the Centre for the major minerals are assigned to the Centre, States lose alternative income accruing activities in these areas where minerals are exploited. Besides, it has to provide both social and physical infrastructure in these areas and in some case the cost of providing them is much higher than in other areas.

Wide disparities in public services follow a pattern. The per capita spending on development expenditures has a significant and positive correlation with per capita GSDP and this is not due to high tax effort of the richer States. This implies that the transfer system has not succeeded in offsetting the fiscal disabilities have resulted in high inter-State disparities in developmental expenditures. The inequalities in per capita expenditures too have shown an increasing trend. Thus inability to place the poorer States on a level playing field in regard to infrastructure provision combined with poor development of market institutions in these States has contributed to growing inter-State inequalities in levels of living. This takes to analyse the equity and efficiency implications of the intergovernmental transfer system.

(c) Intergovernmental Transfers

As mentioned earlier, the founding fathers of the Constitution were aware of the vertical and horizontal fiscal imbalances that can result from the assignment system specified in the Seventh Schedule and under Article 280, provided for the appointment of the Finance Commission within two years of the commencement of the Constitution and thereafter every five years or earlier as may be required.

(i) Encroachment of the role of the Finance Commission:
Table 4
Selected Fiscal Indicators of States 2006-07

<table>
<thead>
<tr>
<th>State</th>
<th>Percapita GSDP</th>
<th>Percapita Development Expenditure</th>
<th>Percapita Own revenues</th>
<th>Per capita Transfers</th>
<th>Per cent of Own Tax to GSDP</th>
</tr>
</thead>
<tbody>
<tr>
<td>Andhra Pradesh</td>
<td>32533.0</td>
<td>4977.2</td>
<td>3788.0</td>
<td>1768.1</td>
<td>9.6</td>
</tr>
<tr>
<td>Bihar</td>
<td>10286.0</td>
<td>2105.3</td>
<td>530.9</td>
<td>1952.9</td>
<td>4.8</td>
</tr>
<tr>
<td>Chhatisgarh</td>
<td>26125.1</td>
<td>4439.6</td>
<td>2974.4</td>
<td>2279.7</td>
<td>9.0</td>
</tr>
<tr>
<td>Goa</td>
<td>95663.5</td>
<td>15460.0</td>
<td>9446.7</td>
<td>2886.7</td>
<td>8.3</td>
</tr>
<tr>
<td>Gujarat</td>
<td>44332.5</td>
<td>4558.4</td>
<td>4056.2</td>
<td>1432.1</td>
<td>7.5</td>
</tr>
<tr>
<td>Haryana</td>
<td>48213.8</td>
<td>5717.8</td>
<td>5736.0</td>
<td>1008.9</td>
<td>9.3</td>
</tr>
<tr>
<td>Jharkhand</td>
<td>23591.2</td>
<td>3992.0</td>
<td>1542.9</td>
<td>1888.3</td>
<td>4.5</td>
</tr>
<tr>
<td>Karnataka</td>
<td>36037.8</td>
<td>5173.7</td>
<td>4567.3</td>
<td>1733.4</td>
<td>11.7</td>
</tr>
<tr>
<td>Kerala</td>
<td>39742.1</td>
<td>4243.7</td>
<td>3841.6</td>
<td>1773.4</td>
<td>9.0</td>
</tr>
<tr>
<td>Madhya Pradesh</td>
<td>18984.1</td>
<td>2872.0</td>
<td>1863.2</td>
<td>1841.9</td>
<td>8.0</td>
</tr>
<tr>
<td>Maharashtra</td>
<td>46307.9</td>
<td>4587.2</td>
<td>4235.6</td>
<td>1383.3</td>
<td>8.2</td>
</tr>
<tr>
<td>Orissa</td>
<td>25997.6</td>
<td>2649.9</td>
<td>1945.3</td>
<td>2568.5</td>
<td>5.7</td>
</tr>
<tr>
<td>Punjab</td>
<td>43436.1</td>
<td>4885.9</td>
<td>4362.7</td>
<td>1612.2</td>
<td>8.5</td>
</tr>
<tr>
<td>Rajasthan</td>
<td>22210.8</td>
<td>3201.1</td>
<td>2301.3</td>
<td>1735.7</td>
<td>8.1</td>
</tr>
<tr>
<td>Tamil Nadu</td>
<td>57635.2</td>
<td>4698.3</td>
<td>4729.4</td>
<td>1454.0</td>
<td>11.4</td>
</tr>
<tr>
<td>Uttar Pradesh</td>
<td>16308.2</td>
<td>2368.9</td>
<td>1607.7</td>
<td>1631.9</td>
<td>8.1</td>
</tr>
<tr>
<td>West Bengal</td>
<td>30739.3</td>
<td>2419.5</td>
<td>1598.7</td>
<td>1550.0</td>
<td>4.8</td>
</tr>
<tr>
<td>Average: Non. Spl. Cat States</td>
<td>28867.0</td>
<td>3606.4</td>
<td>2790.6</td>
<td>1691.0</td>
<td>8.3</td>
</tr>
<tr>
<td>Special Cat. States</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Arunachal Pradesh</td>
<td>27747.5</td>
<td>16941.7</td>
<td>2316.7</td>
<td>17625.0</td>
<td>2.1</td>
</tr>
<tr>
<td>Assam</td>
<td>21947.7</td>
<td>4579.9</td>
<td>1793.1</td>
<td>3749.5</td>
<td>5.6</td>
</tr>
<tr>
<td>Himachal Pradesh</td>
<td>43535.4</td>
<td>7541.5</td>
<td>3690.8</td>
<td>6996.9</td>
<td>5.4</td>
</tr>
<tr>
<td>Jammu &amp; Kashmir</td>
<td>26334.2</td>
<td>8067.3</td>
<td>2279.1</td>
<td>8611.8</td>
<td>6.6</td>
</tr>
<tr>
<td>Manipur</td>
<td>27992.3</td>
<td>9821.7</td>
<td>1195.7</td>
<td>11795.7</td>
<td>1.7</td>
</tr>
<tr>
<td>Meghalaya</td>
<td>28342.6</td>
<td>7399.5</td>
<td>1772.5</td>
<td>8102.9</td>
<td>3.8</td>
</tr>
<tr>
<td>Mizoram</td>
<td>27820.5</td>
<td>16250.0</td>
<td>1820.0</td>
<td>18100.2</td>
<td>2.3</td>
</tr>
<tr>
<td>Nagaland</td>
<td>27740.1</td>
<td>9209.1</td>
<td>918.2</td>
<td>11545.5</td>
<td>1.9</td>
</tr>
<tr>
<td>Sikkim</td>
<td>34820.6</td>
<td>22764.5</td>
<td>4488.1</td>
<td>21177.5</td>
<td>6.4</td>
</tr>
<tr>
<td>Tripura</td>
<td>29500.1</td>
<td>6600.0</td>
<td>1247.1</td>
<td>8108.8</td>
<td>3.5</td>
</tr>
<tr>
<td>Uttarakhand</td>
<td>30956.0</td>
<td>6426.9</td>
<td>3203.2</td>
<td>4154.8</td>
<td>8.2</td>
</tr>
<tr>
<td>Average: Special Cat. States</td>
<td>27189.0</td>
<td>6729.8</td>
<td>2197.1</td>
<td>6375.8</td>
<td>5.6</td>
</tr>
<tr>
<td>Average: All States</td>
<td>28762.5</td>
<td>1962.0</td>
<td>1421.2</td>
<td>1023.9</td>
<td>8.1</td>
</tr>
</tbody>
</table>

Note: GSDP – Gross State Domestic Product.
The mandate of the Finance Commission specified in Article 280 (3) of the Constitution are:

(a) the distribution between the Union and the States of the net proceeds of taxes which are to be or may be divided between them and the allocation between the States of the respective shares of such proceeds;

(b) the principles which should govern the grants in aid of revenues of the States out of the Consolidated Fund of India;

(c) the measures needed to augment the Consolidated Fund of a State to supplement the resources of the Panchayats and Municipalities in the State on the basis of the recommendations made by the Finance Commission of the State; and

(d) any other matter referred to the Commission in the interest of sound finance.

Article 280 (4) further states, “The Commission shall determine their procedure and shall have such powers in the performance of their functions as Parliament may by law confer on them”. The Finance Commission Act also lays down the qualifications of the Chairman and Members of the Commission. While it may not be entirely correct to state that the Governments have always followed them in letter and spirit, the Commissions’ recommendations on tax devolution and grants, by and large, have been implemented.

Thus, the Constitution provides for an impartial semi-judicial body to assess and adjudicate the sharing of resources between the Centre and States, augment the consolidated funds of the States to financially strengthen local governments and to recommend measures on matters referred to it for sustainable fiscal policy calibration. Over the years, however, there have been three important developments, all of which have weakened not merely the Finance Commissions but the entire system of intergovernmental finance. The first relates to the use of “any other matter in the interest of sound finance” as an omnibus provision and loading the Commission with many a term of reference (TOR) to deal with issues it could not grapple with. Within the limited period at its disposal the Commission can not deal with wide ranging matters such as fiscal reform and restructuring programme, tax reforms, expenditure reforms, administrative reforms, debt relief, wage reforms, decentralization reforms, disaster relief and environmental protection. Entrusting the Commission with many tasks has tended to divert the focus of the Commission from its main task.
Not surprisingly, macroeconomic stabilisation concerns have overshadowed developmental concerns in the guidelines issued to recent Commissions. Thus, the Eleventh Finance Commission was asked to review the finances of the Union and the States and suggest ways and means to restructure the public finances to restore budgetary balance and maintain macroeconomic stability and it was asked to design a “monitorable programme of reducing deficits” after it submitted the report. The Twelfth Finance Commission was asked to recommend a fiscal restructuring plan by which both the Union and State governments can phase out their revenue deficits and reduce fiscal deficits to a sustainable level. Similarly, the Thirteenth Finance Commission has been asked to, “….suggest measures for maintaining a stable and sustainable fiscal environment consistent with equitable growth”. Although ensuring macroeconomic stability is an important objective and it is appropriate for the Finance Commissions to take sustainability into account while recommending transfers, it is questionable whether it should be the primary focus. Stabilisation function is predominantly in the domain of the Union government and assigning primacy to this task relegating distribution of fiscal resources as secondary could create difficulties for both development and inter-regional equity. When the Finance Commissions’ transfers fail to fully offset the fiscal disabilities and when for macroeconomic stability reasons uniform borrowing caps are prescribed as was done by the 12th Finance Commission, the pattern of development could be severely distorted threatening the stability of the federation itself. Uniform fiscal deficit target enables the poorer States to borrow much lower amounts in per capita terms. In the event, they can not match the more affluent States in providing social and physical infrastructure and this imbalance causes imbalance in the flow of private investments and accentuates inter-State disparities in development.

The second important development is that over the years Article 280 (d) has been used not only to load additional tasks but also to restrict the scope of the Commission. The most important encroachment was in restricting its scope to non-plan revenue accounts of the States. The first and second Commissions did not have the problem as the plan process had just been started then. Although the third Commission was asked to take account of the plan side, the government rejected the majority recommendation taking account of the 75 per cent of the plan expenditure and accepted the minute of dissent by the Member-Secretary of excluding the plan side altogether. The Fourth Commission was specifically asked not to take account of plan expenditures, the Commission was

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22 This is one of those rare cases where the Government did not accept the majority recommendation of the Commission.
more than willing to vacate the field when it stated, “… The Constitution does not make any distinction between Plan and non-Plan expenditure and it is not unconstitutional for the Finance Commission to go into the whole question of the total revenue expenditure of the States….”, it decided that “…it would not be appropriate for the Finance Commission to take upon itself the task of dealing with the States’ new Plan expenditure”.

The Fifth Finance Commission was specifically excluded from taking into account plan expenditures. Subsequently, except for the Ninth and the Thirteenth Commissions, the TOR confined the role of the Commissions to assessing non-plan revenue side requirements of the States. Taking such a lopsided view of the requirements has not done any good to the Constitutional mandate of the Commission.

The third important development is the issue is the emergence of multiple agencies and overlapping roles in giving transfers. In fact, the ability of the Finance Commission to offset the fiscal disabilities of the States lies in defining its own scope and understanding the constraints it has in undertaking its task. There are two important developments in the transfer scene. First, the capacity of the Finance Commission to achieve the desired degree of equalisation is constrained by the Planning Commission and various Central Ministries making grants for both general and specific purposes under Article 282. Obviously, the Finance Commission does not have any control over the distribution of transfers under these heads.

Second, the transfer system as a whole has become more and more discretionary. Increased discretion in the transfer system was aided by the extensive use of Article 282 to give grants not only for State plan schemes on the basis of the formula determined by the National Development Council but also for various Central sector and centrally sponsored schemes by different ministries. These transfers are for specific purposes with or without matching requirements initiated by central ministries to claim ownership to various schemes in a fragmented polity and by-passing the States in making transfers for areas under the States’ domain. In fact, many of these transfers passed through the State budgets until 2002-03, but thereafter, the Centre has been giving the grants directly to implementing agencies bypassing the States which has brought in the questions of monitoring and accountability. Analysis shows that the proportion of transfers made through Finance Commissions’ recommendations have stagnated in spite of significant proportion of grants being given directly to implementing agencies bypassing the States (Table 5) and even

\[23\] See footnote 2 above.
more important, the formula based transfers have significantly declined as formula based transfers constitute just about 26 per cent even under transfers under the State plan schemes as compared to over 80 per cent a decade ago. Even under the State Plan grants, the normal assistance given under the Gadgil formula declined from 85 per cent of State Plan assistance in 1991-92 to 27.5 per cent in the 2008-09 budget. The consequence of these developments are: (i) the Finance Commission can not take a holistic view on public service provision in its transfer scheme; (ii) meeting the objectives of the transfers in the prevailing system is extremely difficult and (iii) increase in the discretionary component reduces objectivity and credibility of the transfer system.

The founding fathers of the Constitution, in order to ensure that the States should not be made to depend on the munificence or arbitrary will of the Centre constructed a scheme of transfers involving articles 275 and 280 (3). The wording of the Article 280 that the “President shall appoint a Finance Commission” and the Commission shall make recommendations to the President entrusts the Commission the role of a Constitutional authority to deal with the task of effecting a fair distribution of resources.

While presenting his views to the Ninth Finance Commission, Mr. K. K. Venugopal persuasively argues that both the positive interpretation of Article 275 and analysis of the non-obstante clause of Article 282 lead to the conclusion that the prevailing practice is contrary to the Constitutional provisions.24 The positive construction of Article 275 shows that the Central Government can give all types of grants - general purpose or specific purpose, conditional or unconditional and revenue or capital grants. As Article 275 grants are given on the recommendation of the Finance Commission, the latter is fully competent to make recommendations on all the above. At the same time, it is not possible to visualise Article 282 as a miscellaneous provision for giving grants from the Centre to the States. The non-obstante clause of the Article states, “…Notwithstanding that the purpose is not one with respect to which Parliament or the legislature of the State, as the case may be, may make laws”. According to Mr. K. K. Venugopal, this Article is meant to lift the bar for both the States and the Centre to make grants for any public purpose to institutions on subjects outside their legislative purview as listed in the Union and State lists. Mr. Venugopal’s interpretation is that Article 282 can not be construed as a miscellaneous provision because it visualises that the grantors could either

be the Union or a State. In his view, “…to the extent that any of the terms of reference seek to deprive the Finance Commission of its powers which are constitutionally vested in it under Article 280, Clause 3, the terms would be invalid and unconstitutional” (NIPFP, 1993; p. 274).

Whether legitimate or otherwise, the development over the years have led to taking a segregated view of the States’ requirements with Finance Commission concerned with only maintenance expenditures, Planning Commission dealing with spending on new services and various central ministries spending on various schemes. This has led to a number of undesirable outcomes. First, there is a serious disconnect between creation and maintenance expenditures and poor planning for public service delivery. Second, the multiple agencies pursue their own goals and this has prevented a holistic treatment of equalisation. Third, the preference to show large plan expenditures has led to significant under provision for maintenance resulting in low productivity. Fourth, the system has opened up scope for arbitrariness and discretion as over the years, formula based transfers have shown a steady decline. The schematic transfers have invaded even the grants under State Plan Schemes and formula based transfers within the State Plan Schemes now constitute a mere 26 per cent of the total transfers.

**Table 5**

**Composition of Central Transfers to States**

<table>
<thead>
<tr>
<th>Plan Periods/ Years</th>
<th>Finance commission Transfers</th>
<th>Plan Grants</th>
<th>Other Grants Total</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Tax Devolution</td>
<td>Grants</td>
<td>Total</td>
</tr>
<tr>
<td>Fourth Plan</td>
<td>54.4</td>
<td>10.3</td>
<td>64.6</td>
</tr>
<tr>
<td>Fifth Plan (1974-79)</td>
<td>50.2</td>
<td>17.1</td>
<td>67.3</td>
</tr>
<tr>
<td>Sixth Plan (1980-85)</td>
<td>57.0</td>
<td>5.1</td>
<td>62.1</td>
</tr>
<tr>
<td>Seventh Plan (1985-90)</td>
<td>54.2</td>
<td>6.9</td>
<td>61.0</td>
</tr>
<tr>
<td>Annual Plan (1990-91)</td>
<td>52.2</td>
<td>10.5</td>
<td>62.7</td>
</tr>
<tr>
<td>Eighth Plan (1992-97)</td>
<td>55.2</td>
<td>6.1</td>
<td>61.8</td>
</tr>
<tr>
<td>Ninth Plan (1997-2001)</td>
<td>58.7</td>
<td>6.0</td>
<td>64.7</td>
</tr>
<tr>
<td>Tenth Plan (2002-2007)</td>
<td>55.4</td>
<td>9.8</td>
<td>65.2</td>
</tr>
</tbody>
</table>

**Note:** Figures in parenthesis are percentages to total transfers.

**Source:** State Finances – A Study of Budgets (various years), Reserve Bank of India Bulletin
(ii) Finance Commission Transfers:

As mentioned earlier, although the Constitution does not place any restriction on the scope of the Finance Commission, it has come to be restricted to meeting the non-plan current expenditure requirements of the States. The approach of the Finance Commissions to transfers consists of (a) assessment of overall budgetary requirements of the Centre and States to determine the volume of resources that can be transferred during the period of their recommendation; (b) forecasting States’ own current revenues and non-plan current expenditures; (c) determining the States’ share in Central tax revenues and distributing this share among the States; (d) filling the post-devolution projected gaps between non-plan current expenditures and revenues with the grants in aid. This has come to be known as the “gap-filling” approach.

Prior to the Constitutional amendment in which devolution of certain central taxes was replaced by general tax sharing, the Finance Commissions were required to recommend the transfer of additional excise duties in respect of sales taxes on sugar, textiles and tobacco. In respect of these three groups of articles, the States had voluntarily surrendered their right to levy sales taxes and the Centre has been levying additional excise duties, which was passed back to States on the basis of origin as recommended by the Commission. With the substitution of general tax sharing for sharing of individual taxes, separate assignment of additional excise duties was discontinued. The Twelfth Finance Commission recommended the distribution of 31.5 per cent of net proceeds of Central taxes consisting of 30 per cent for general tax sharing and 1.5 per cent in lieu of additional excise duties. The entire 31.5 per cent is to be distributed according to a uniform formula given in Table 6.

### Table 6

<table>
<thead>
<tr>
<th>Criteria and Weights for Tax Devolution</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Population</strong></td>
</tr>
<tr>
<td><strong>Income Per Capita (Distance Method)</strong>*</td>
</tr>
<tr>
<td><strong>Area</strong></td>
</tr>
<tr>
<td><strong>Index of Infrastructure</strong></td>
</tr>
<tr>
<td><strong>Tax Effort</strong>**</td>
</tr>
<tr>
<td><strong>Fiscal Discipline</strong>***</td>
</tr>
</tbody>
</table>

Note: *The distance method is given by: \((Y_h - Y_i)P_i / S(Y_h - Y_i)P_i\), where, where, \(Y_i\) and \(Y_h\) represent per capita SDP of the \(i^{th}\) and the highest income State respectively and \(P_i\) is the population of the \(i^{th}\) State.

**Tax Effort \((h)\) is estimated as \((h) = (T_i / Y_i) / 0.5 (1/Y_i)\) where, \(T_i\) is the per capita tax revenue collected by the \(i^{th}\) State and \(Y_i\) is the per capita State domestic product of the \(i^{th}\) State.

***Estimated as the improvement in the ratio of own revenue of a State to its revenue expenditures divided by a similar ratio for all States averaged for the period 1966-99 over 1991-1993.
An important feature of tax devolution recommended by the Finance Commissions is that, while the criteria adopted for distribution are different from the principles of grants-in-aid, nowhere is it made clear that the economic objectives of the two instruments are different (Rao and Sen, 1996, Ch.6). The tax devolution is recommended mainly on the basis of general economic indicators (Table 6) and grants are given to offset the residuary fiscal disadvantages of the States as quantified by the Commissions. Further, assigning weights to contradictory factors like ‘backwardness’ and ‘contribution’ in the same formula has rendered the achievement of the overall objective of the transfer system - offsetting revenue and cost disabilities difficult.

Over the years, attempts have been made to improve degree of equalisation in the transfer scheme by assigning larger weights to per capita SDP either in the “inverse” or “distance” formulations by the successive Commissions. Yet, population has continued to receive the largest implicit and explicit weight. Equally important is the unreliability of tax effort and index of fiscal discipline. In a tax system which is predominantly origin based, there can be significant inter-State tax exportation and the tax effort indicator ignores this phenomenon. Besides, there are a number of other factors in addition to per capita SDP that determine the taxable capacity of a State. The changes in the ratios of own revenues to revenue expenditures relative to all-State average and their changes over time can occur due to factors totally extraneous to States’ own efforts at fiscal discipline.

Equalisation has been further blunted by the terms of reference, which require the Commissions to use the 1971 population figures in the transfer formula. The TOR for the Finance Commissions stipulates that they should use 1971 population figures whenever they use this as an indicator for tax devolution. This is according to the National Population Policy adopted in 1976 which required freezing of the population figures at 1971 level in allocation of central assistance to States, devolution of taxes and duties and grants-in-aid up to the year 2001. The National Population Policy adopted in 2000 extended the freeze until 2026. The ostensible reason for this is to penalise the States with higher population growth rates. It must be noted that population growth in the State is the consequence of fertility rate and net migration. Thus, taking 1971 population figures in the formula for tax devolution would penalise not only the States with high fertility rates but also those with high migration, and this goes against the principles of federalism itself. The important questions are first, whether, the federal transfer mechanism should be employed as an instrument of population policy and second, even if it is, why should this provide a disincentive against population migration from one State to another.
As mentioned earlier, the post devolution gaps between projected revenues and non-plan revenue expenditures are filled through the grants by the Finance Commissions under Article 275 and this is characterised as the “gap-filling” approach of the Commissions. This approach has attracted two major criticisms. First, the approach and methodology of the commission creates the “tyranny of the base year”. Projections are made after firming up the data on the base year and if a State has low per capita expenditures in the base year, the projections are made from this low base and not what the State requires. Even if the growth rate assumed is marginally higher for the States with low base year expenditures, it is impossible to offset the fiscal disability of the State due to low revenue raising capacity. Notably, while tax devolution is determined on the basis of general economic indicators, grants are given on the basis of projected post-devolution budgetary gaps. Thus, the Finance Commission transfers are not designed specifically to offset fiscal disadvantages of the States arising from lower revenue raising capacity and the higher unit cost of public services. The second and equally important criticism is the perverse incentives on the fiscal management the transfer system creates. The “fiscal dentistry” – filling budgetary cavities with the grants has the incentive that can show a larger gap gets larger grants. In other words, the States can afford not to tax their residents to their capacity and indulge in expenditure profligacy to get larger grants and pass on the burden of this profligacy to the national tax payer.

There has been considerable concern by the Finance Commissions about following the “gap-filling” approach. This was the reason for modifying the terms of reference of the Ninth Finance Commission to follow a “normative approach”. The Commission made an attempt to estimate fiscal capacities and needs of the States but used the results of the exercise only partially in making its recommendations on grants. The Tenth and subsequent Commissions, simply abandoned the approach. The 11th Finance Commission in the additional terms of reference given to it just before the finalisation of its recommendations was asked to “…draw a monitorable fiscal reforms programme aimed at reduction of revenue deficit of the State and recommended the manner in which the grants to the States to cover the assessed deficit in their non-plan revenue account may be linked to progress in implementing the programme.”

The 11th Commission worked out a scheme by pooling 15 per cent of revenue deficit grants and adding an equal amount to it to create an incentive fund to be allocated among the States based on fulfilment targets of growth of tax and non-tax revenues and expenditures on salaries, interest payments and subsidies set in the fiscal restructuring
plan detailed by the Commission. It gave equal weight to monitorable measures on the revenue and expenditure sides and specified weights to each of the monitorable measures. The incentive fund was allocated to the States according to their population shares. A State would receive the full amount if it fulfilled the targets and the amount would vary depending on the degree of achievement of monitorable targets. If a State did not get the full amount during the first four years, the residual would continue to be available in subsequent years, but if by the fifth year the targets are not achieved, the funds would lapse. To implement this scheme a monitoring agency should be set up by the Government of India consisting of representatives of the Planning Commission, Finance Ministry and representatives of State governments.

There are a number of problems with the proposed scheme. Some of them have been pointed out in the Note of Dissent presented by one of the Members of the Commission (Government of India, 2000, pp. 9-13). There are concerns both with the monitorable measures and implementation mechanism. The measures can vary not only due to factors within the States’ control but also because of factors beyond their control. There are also problems of fiscal autonomy of the States when its actions are supervised by a monitoring agency. Finally, while the scheme tries to monitor the fiscal performance of the States, there is no mechanism to monitor the performance of the Centre. Not surprisingly, after a detailed analysis, the Twelfth Finance Commission recommended the discontinuation of the scheme. Instead, it tried to incentivize the fiscal performance of the States by designing the debt restructuring scheme. The States passing the fiscal responsibility legislation and presenting the medium term expenditure framework agreeing to phase out the revenue deficits and compress fiscal deficits to 3 per cent of their gross State Domestic Product (GSDP) were given the benefit of debt rescheduling at a lower interest rate (7.5 per cent) and the progress in reduction in revenue deficits was linked to write off of the debt repayable to the Central Government by an equal magnitude.

The Twelfth Finance Commission too followed the methodology followed by the previous Commissions. In addition, it tried to provide equalization grants for elementary education and healthcare. It worked out the norms for expenditure requirements in these sectors by taking per capita expenditures on the service at all State average share of expenditures on the sector in total. For this purpose, the Commission included both plan and non-plan

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expenditures. Based on this, expenditure requirements for each State is worked out and the difference between the requirements and actual expenditures was taken as the grant requirement. However, the Commission found that it could not give the Commission could not give the grants to fully equalise the expenditure levels. It recommended the grant equal to cover 15 per cent of the shortfall in the case of education and 30 per cent of the shortfall in the case of health sector.

While the intention to equalise the standards of basic services such as elementary education and healthcare is commendable, there are serious problems with the design of the transfer system. Firstly, there are already a number of specific purpose grants given under the centrally sponsored schemes and this is yet another scheme. Even thought the commission States that it has taken all plan and non-plan expenditures in estimating the requirements, the way in which the various grants for the sector are administered makes it difficult to monitor the performance any grant component in terms of outputs and outcomes. Furthermore, the education and health sector grants are given under the major head on education and there is nothing in the system to prevent a State from incurring expenditures on higher education instead of elementary education. More importantly, after the elaborate exercise to estimate expenditure needs, it is ironical that the Commission could not find resources to equalise the expenditure requirements completely. This implies that the Commission willingly left the requirements calculated by itself uncovered! Third, the Finance Commission does not have a system of monitoring specific purpose grants nor did it recommend a specific way to monitor the same. In the event, it is doubtful whether the intended equalisation even in expenditures is likely to be brought about.

It is important also to note that the focus of the Twelfth Finance Commission's fiscal restructuring plan was macroeconomic stability even if it meant sacrificing development in fiscally disadvantaged States. The reference is to the uniform targets given to the States to eliminate their revenue deficits and reduce fiscal deficits to 3 per cent of GSDP. Given the low levels of expenditures on social and physical infrastructure in poorer States, achieving the fiscal restructuring targets further entailed compressing their productive expenditures. Thanks to the acceleration in the growth of the economy to over 8 per cent since 2003-04, and very high buoyancy of Central revenue collections and consequently, buoyant central transfers, the States with the exception of Kerala, Punjab and West Bengal have been able to make the necessary corrections as per the fiscal restructuring plan.
(iii) **Formula based transfers for State Plan Schemes:**

Until 1969, both the volume of Central assistance and its grant-loan components were given to the States based on the nature of the projects approved under the State Plans. However, since 1969, these are given on the basis of a formula determined by the National Development Council (Gadgil formula) which is summarised in Table 6. Until 2004-05, the plan assistance was given in terms of grants as well as loans. Of the total assistance, 30 per cent was kept apart for the special category States and distributed among them on the basis of plan projects formulated by them. For these States, 90 per cent of the assistance was as grants and the remaining as loans. The 70 per cent of the funds available for the non-special category States is distributed in the ratio of 30 per cent grants and 70 per cent loans. Since 2005-06 however, the practice of giving plan assistance to States as loans has been discontinued, based in the recommendation of the Twelfth Finance Commission to ensure better fiscal discipline. Thus, while the formula continues to be used for distributing plan grants to States, the loan proportion has to be availed from the market.

<table>
<thead>
<tr>
<th>Variable</th>
<th>Weight</th>
</tr>
</thead>
<tbody>
<tr>
<td>Population (1971)</td>
<td>60.0</td>
</tr>
<tr>
<td>1. Per capita SDP, of which,</td>
<td></td>
</tr>
<tr>
<td>(i) Deviation from the average to the States below average per capita SDP</td>
<td>20.0</td>
</tr>
<tr>
<td>(ii) ‘Distance ‘ from the highest per capita SDP for all the general category States</td>
<td>5.0</td>
</tr>
<tr>
<td>2. Fiscal Performance, of which,</td>
<td></td>
</tr>
<tr>
<td>(i) Tax effort</td>
<td>2.5</td>
</tr>
<tr>
<td>(ii) Fiscal management</td>
<td>2.5</td>
</tr>
<tr>
<td>(iii) National objectives</td>
<td>2.5</td>
</tr>
<tr>
<td>3. Special Problems</td>
<td>7.5</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>100.0</td>
</tr>
</tbody>
</table>

**Note:**

1. The formula is applied to general category States. They receive 70 per cent of the total plan assistance of which, 30 per cent is given as grants and the remaining, loans.
2. The Special category States receive 30 per cent of total plan assistance and the distribution is done according to the plan projects approved in the States.

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26 The formula and its modifications from time to time are evolved on the basis of consensus in the NDC. The NDC is constituted by the cabinet ministers at the Centre, chief ministers of the States and the Members of the Planning Commission and is chaired by the Prime Minister.
The analysis of the formula shows that overwhelming proportion of the assistance is given on the basis of population, with a 60 per cent weight assigned to (60 per cent) population, and the weight to backwardness as measured by per capita GSDP was 25 per cent. This implies that the plan transfers too are not designed to offset fiscal disabilities of the States. In other words, plan grants are not linked to infrastructure requirements of different States, nor does it have any relationship with the actual plan investments of the States.

It is important to note that over the years, discretionary component has engulfed the State plan assistance as well. Until the mid 1990s, the State plan assistance was given mostly according to the Gadgil formula. However in more recent years, formula (Gadgil Formula) based assistance under the State Plan schemes has from 85 per cent of the total State Plan assistance in 1991-92 to less than 30 per cent in the 2008-09 budget (Figure 1).

(iv) Assistance to the Central Sector and Centrally Sponsored Schemes:

The third component in the transfer system is the specific purpose grants given to the States for central sector and centrally sponsored schemes. These grants are conditional, many of the shared cost schemes with varying matching requirements. Despite attempts at consolidating them the number of schemes remains large and it is difficult to keep a track on them. These transfers have attracted the sharpest criticism due to their discretionary
nature and conditionality attached to them and yet, both Central and State governments have enabled their steady increase. They accounted for about 60 per cent of the total plan assistance and about 20 per cent of total current transfers were given to these schemes in 2000-01. As mentioned earlier, these constitute over 70 per cent of even the State plan grants besides the central schemes. Although the intention is to ensure minimum standards in respect of these meritorious services\textsuperscript{27}, and many are distributed according to the requirements as indicated by service levels, as some States do not avail their entitlements fully, and in fact, in many cases, moneys are received late in the year, the administering ministry redistributes the money saved to those more enterprising States which can produce utilisation certificates to ensure that they spend the money allocated to the programme within the financial year. In the event, the actual pattern of distribution is entirely different from the original allocation. Since 2003-04, the grants to a number of these schemes are given directly to implementing agencies bypassing the States and the volume of assistance thus given constituted Rs. 87054 Crore or 1.6 per cent of GDP in 2008-09.

With this, there is no place at the State level to consolidate spending on basic services such as education, healthcare, poverty alleviation and urban renewal as the funds for central schemes go directly to the implementing agencies. Many States seem to have interest in the schemes, but only to claim ownership to them. When it comes to the question of monitoring them, the responsibility is shifted to the Centre. As far as the Central Government is concerned, it claims ownership to the schemes, but is unable to monitor them nor is it able to institute a proper system of accountability. Many times, the implementing agencies do not have accountability to elected representatives as well.

(iv) Financing infrastructure at the State level: Loans.

For macroeconomic reasons, the Constitution places limitation on the borrowing powers of the State governments. Art. 293 of the Constitution extend the States’ power to borrow within the territory of India and provide guarantees for the borrowing by other entities within the limits prescribed by the State Legislature. The provisions of the Article also enable Government of India to make loans to the States and give guarantees in respect of loans raised by any State subject to the limitation fixed by the Parliament by law, from

\textsuperscript{27} Martin Feldstein (1975) calls them categorical equity goods.
the Consolidated Fund of India. However, when a State is indebted to the Union
government, it is required to take the consent of the latter for raising loans.

The development of public finance in the country in the context of planned development
strategy has resulted in all the States being indebted to the Centre. Article 293 of the
Constitution empowers the States access to market borrowing. However, if a State is
indebted to the Centre, it must have Central permission before borrowing. Until 2004-05,
plan assistance to the States was given in the mix of grants and loans and this has ensured
that every State is indebted to the Centre. In addition, non-plan loans are also given to
meet certain exigencies. Often the ways and means loans given by the Reserve Bank of
India for meeting liquidity problems are converted into medium term loans by the Central
Government. Therefore, the market borrowing of the States virtually boils down to the
Union Ministry of Finance, the Planning Commission and the Reserve Bank of India
determining the quantum of borrowing to be allowed to each State every year.

The Reserve Bank of India, as a banker to the Government takes the bonds and passes
them on to the commercial banks and the latter are required to invest a stipulated
proportion of their demand and time liabilities in government bonds (statutory liquidity
ratio). There is a small proportion of the borrowing allowed to float in the market.
There are no clear rules or norms for determining fresh borrowing of the States, but
considerations such as the volume of repayment and need to have a reasonable plan size
and the prevailing volume of indebtedness in each State are factors taken into account in
determining the market borrowing. Presently, as 26 of the 28 States have passed the
fiscal responsibility legislations limiting their fiscal deficit to 3 per cent in 2009-10, it has
become easier to make market borrowing allocations. Given the ceiling of fiscal deficit,
the volumes of net small saving and provident fund collections in each State would have
to be estimated and the remaining has to largely come from market borrowings. As in the
future, the Finance Commission will fix the ceiling on fiscal deficit for each States, allocation
of market borrowing will not pose serious difficulties.

In a competitive market economy, States’ developmental effort should be supplemented
by the development of the bond market which should not only act as States’ barometer
of credit worthiness and should ensure adequate flow of resources for their infrastructure
development. This would, of course, result in bonds of different States carrying different
rates of interest depending upon the risk perceptions and their credit worthiness. As the
bond market is developed, the over-reaching role of the Central Government in lending
resources to the States as well as in controlling their market borrowing will have to ease and greater market discipline and regulation will have to be instituted. This may call for a re-examination of the constitutional provisions relating to the State’s borrowings. It is therefore important to know the extent to which the Central control over State’s borrowing should be replaced by market discipline and at what pace such a reform should be instituted.

(vi) Equalising Effect of Intergovernmental Transfers:

In this section, an attempt is made to analyse the degree of equalization of the three sources of intergovernmental transfers. We have argued that the methodology adopted by the Finance Commissions does not offset the fiscal disabilities of poorer States adequately to enable them to make comparable levels of investments in social and economic infrastructure. Similarly the plan transfers too are not targeted to offset fiscal disabilities. Both these are in the nature of unconditional general purpose transfers and they are given to enable every State to provide comparable levels of public services at comparable tax rates. In contrast, the grants given for central sector and centrally sponsored schemes are meant to ensure that for specified services which are considered meritorious, a stipulated minimum expenditure must be incurred to ensure minimum standards of services in respect of them.

It must be noted that the objective of the intergovernmental transfer system is not to equalising incomes of different states but simply to offset their fiscal disabilities arising from low revenue raising capacity and higher unit cost of providing public services. The ultimate objective is to enable every state to provide comparable levels of public services at comparable tax rates. However, in the following exercise, the evaluation of equalization is attempted using income as the barometer because it represents taxable capacity. Given that taxable capacity of the States depends on their per capita incomes, the progressivity of the transfer system is examined with respect to per capita incomes of different states.

The empirical analysis presented in Table 8 shows the degree of equalization from each of the three sources of transfers. It is seen that despite our general criticism that the Finance Commissions’ transfers are not designed to offset shortfalls in revenue capacity and high unit costs of providing public services, they are the most equalising among the three different transfer categories. The log-linear regressions of per capita transfers on

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28 Horizontal equity requires that every individual irrespective of the State he lives should have entitlement to comparable standards of public services so long as he pays taxes at comparable rates. See Buchanan (1950); Boadway and Flatters (1982).
per capita GSDP for the cross section of non-special category States (excluding the small State of Goa) in 2005-06 shows that only the Finance Commissions have a significant equalising impact with the elasticity of -0.53 largely due to the progressive distribution of tax devolution recommended by the Twelfth Finance Commission. Grants for State Plan as well as Centrally Sponsored Schemes do not have significant equalisation impact and the equalization seen in the transfer system is mainly due to Finance Commission transfers.

Table 6
Equalization in Fiscal Transfer System in India – 2005-06

<table>
<thead>
<tr>
<th>1. Major States</th>
<th>Finance Commission</th>
<th>Plan Transfers</th>
<th>Total Transfers</th>
</tr>
</thead>
<tbody>
<tr>
<td>2. State Plan Schemes</td>
<td>4.9104* (2.9939)</td>
<td>3.9331 (1.3682)</td>
<td>11.1025* (8.7866)</td>
</tr>
<tr>
<td>3. Centrally Sponsored Schemes</td>
<td>0.0177 (0.0966)</td>
<td>0.0177 (0.0966)</td>
<td>0.0177 (0.0966)</td>
</tr>
</tbody>
</table>

Note: Estimated by employing the functional form: \( \ln G = a + b \ln Y + \hat{\epsilon} \)
Where, \( G \) denotes different types of per capita transfers, \( Y \) represent per capita GSDP, \( a \) and \( b \) represent parameter estimates and \( \hat{\epsilon} \) is the error term.
* Significant at 1 per cent level.

The inability to offset fiscal disabilities has resulted in the low income states spending substantially lower per capita expenditures on developmental heads. The analysis of expenditures on basic social and economic services presented in Table 8 shows that inter-State differences in per capita expenditures are not only high but have increased. The analysis is carried up to 2003-2004 because in subsequent years, the Central Government has been giving transfers for many of the central schemes directly to the implementing agencies bypassing the States. The coefficients of variation in per capita expenditures in education, health as well as on economic services have shown a steady increase during the last decade. It is also seen that per capita expenditures on education, health, total social services, and economic services as well as aggregate expenditures has always been
high and significant. Together with increasing coefficients of variation, these results show that per capita expenditures are higher in high income States and differences in per capita expenditures between low income and high income States have steadily increased over the years.

Inequalities in the spending cause inequalities in the access to basic social and economic services. Thus, children in States with low literacy rates have poor access to school education and people in States with low health status have low levels of expenditures on healthcare. Similarly the States with low infrastructure levels have low expenditures on infrastructure facilities. This pattern of spending accentuates unequal access to social and physical infrastructure accentuating inequalities in levels of living and human development in the States.

Inability to offset the fiscal disabilities has resulted in high inter-State disparities in developmental expenditures. There is a very high correlation between per capita development expenditures and per capita incomes of the States and this can not be explained by differences in own revenues raised. The inequalities in per capita expenditures too have shown an increasing trend. Thus inability to place the poorer States on a level playing field in regard to infrastructure provision combined with poor development of market institutions in these States has contributed to growing inter-State inequalities in levels of living.
Table 8
Inter-State Differences in Expenditures on Public Services

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Education</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>a. Mean (Rs)</td>
<td>285.79</td>
<td>532.06</td>
<td>522.69</td>
<td>531.31</td>
<td>550.18</td>
</tr>
<tr>
<td>b. Coefficient of Variation</td>
<td>0.35</td>
<td>0.45</td>
<td>0.40</td>
<td>0.47</td>
<td>0.48</td>
</tr>
<tr>
<td>c. Corr. Coeff with Per capita NSDP</td>
<td>0.616</td>
<td>0.644</td>
<td>0.619</td>
<td>0.699</td>
<td>0.513</td>
</tr>
<tr>
<td>2. Medical and Public Health</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>a. Mean</td>
<td>88.33</td>
<td>146.42</td>
<td>146.93</td>
<td>148.42</td>
<td>154.99</td>
</tr>
<tr>
<td>b. Coefficient of Variation</td>
<td>0.27</td>
<td>0.45</td>
<td>0.36</td>
<td>0.34</td>
<td>0.35</td>
</tr>
<tr>
<td>c. Corr. Coeff with Per capita NSDP</td>
<td>0.687</td>
<td>0.765</td>
<td>0.793</td>
<td>0.811</td>
<td>0.528</td>
</tr>
<tr>
<td>3. Social Services</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>a. Mean</td>
<td>575.48</td>
<td>1030.51</td>
<td>1033.23</td>
<td>1060.39</td>
<td>1136.11</td>
</tr>
<tr>
<td>b. Coefficient of Variation</td>
<td>0.40</td>
<td>0.42</td>
<td>0.32</td>
<td>0.33</td>
<td>0.37</td>
</tr>
<tr>
<td>c. Corr. Coeff with Per capita NSDP</td>
<td>0.841</td>
<td>0.763</td>
<td>0.812</td>
<td>0.852</td>
<td>0.716</td>
</tr>
<tr>
<td>4. Economic Services</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>a. Mean</td>
<td>514.74</td>
<td>827.85</td>
<td>821.69</td>
<td>854.21</td>
<td>1128.96</td>
</tr>
<tr>
<td>b. Coefficient of Variation</td>
<td>0.38</td>
<td>0.58</td>
<td>0.49</td>
<td>0.42</td>
<td>0.34</td>
</tr>
<tr>
<td>c. Corr. Coeff with Per capita NSDP</td>
<td>0.824</td>
<td>0.765</td>
<td>0.671</td>
<td>0.740</td>
<td>0.662</td>
</tr>
<tr>
<td>5. Development Expenditure</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>a. Mean</td>
<td>1090.23</td>
<td>1858.36</td>
<td>1854.92</td>
<td>1914.61</td>
<td>2265.07</td>
</tr>
<tr>
<td>b. Coefficient of Variation</td>
<td>0.33</td>
<td>0.47</td>
<td>0.37</td>
<td>0.36</td>
<td>0.30</td>
</tr>
<tr>
<td>c. Corr. Coeff with Per capita NSDP</td>
<td>0.872</td>
<td>0.794</td>
<td>0.791</td>
<td>0.828</td>
<td>0.865</td>
</tr>
<tr>
<td>6. Total Expenditure</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>a. Mean</td>
<td>1690.37</td>
<td>3059.30</td>
<td>3180.46</td>
<td>3348.41</td>
<td>3858.04</td>
</tr>
<tr>
<td>b. Coefficient of Variation</td>
<td>0.37</td>
<td>0.45</td>
<td>0.34</td>
<td>0.36</td>
<td>0.31</td>
</tr>
<tr>
<td>c. Corr. Coeff with Per capita NSDP</td>
<td>0.885</td>
<td>0.842</td>
<td>0.917</td>
<td>0.905</td>
<td>0.839</td>
</tr>
</tbody>
</table>

Not surprisingly, inter-State disparities among the general category States are not only high, but have shown an increasing trend (Rao, 2008, 2009). In 1980-81, the per capita SDP in the richest State, Punjab (Rs. 2674) was about 2.9 times that of the poorest, Bihar (Rs. 919). In 2006-07, this difference increased to 4.8 times with per capita SDPs of
Haryana, the highest income State at Rs. 48214 and Bihar at Rs. 10286 (Table 4). It is also seen that per capita income levels have tended to diverge sharply after market based reforms were initiated. (Rao et. al., 1999). With economic liberalization in 1991, the States with better market development and better transport infrastructure and connectivity could take greater advantage of the opportunities than those with poor transport infrastructure and low levels of market development.

(d) Institutional Mechanism for Intergovernmental Transfers

Keeping in view the need to evolve a transparent and an impartial system of transfers to ensure that the financial strength of the Centre and the States are on an even keel, the Constitution provided for the appointment of the Finance Commission. As the Commission was to be appointed every five years, the mechanism provided for taking account of the changing needs and norms of the Centre and the States. The Finance Commission (miscellaneous) Act also lays down qualifications of the Chairman and Members of the Commission and the presence of a judicial member/chairman in the Commission is supposed to give it a semi-judicial status. The provision for setting up the Finance Commission has been on the lines of the Commonwealth Grants Commission in Australia, through there are important differences both their status and working.

Despite the provision of a specialised independent and semi-judicial agency, it would be difficult to pronounce that the intergovernmental institutions have helped to evolve a satisfactory system of fiscal transfers. The shortcomings of the institutional mechanism are seen in a number of ways. First, as already mentioned, although the Constitution envisaged a rule based transfers on the recommendation of the Finance Commissions, developments have contrived to reduce the constitutional body to a minor role and a major proportion of transfers lies outside its purview. The multiple agencies giving transfers in an uncoordinated manner cannot be expected to singularly pursue economic objectives of intergovernmental transfers. Besides, while the Finance Commission is expected to be a non-political body, the Planning Commission is not. The Gadgil formula used for distributing Plan assistance is determined by consensus in the national Development Council where all the States are members and it would be unrealistic to expect targeted transfers to offset fiscal disadvantages in such a system. The Centrally Sponsored Schemes in any case are discretionary, designed by the Central Ministries where many non-economic considerations enter into the distribution mechanism.

Although the Finance Commission is expected to be a non-political body, political
considerations play an important role in the appointment of the Chairman and Members of the Commission, in specifying their terms of reference and in the functioning of the commission itself (Rao and Sen, 1996). In selecting the Chairman and Members of the Commission and specifying its terms of reference, the Central Government, more particularly the Union Ministry of Finance plays a leading role, and this raises questions about their objectivity and fairness in the minds of the States. This is particularly true when political personalities are appointed to the Commission. In addition, the Member-Secretary/Secretary is always a senior bureaucrat belonging to the IAS, who will be appointed not because of his expertise or interest in the subject, but merely because he qualifies to be appointed as a Secretary to Government of India. Often, mid-way through the Commission’s tenure, the Member-Secretary secures transfer to regular posting as the Secretary in an important Ministry\(^1\). The staff of the Commission, by and large, also comes on deputation from various Central ministries and most of them are not familiar with the technical requirements of determining intergovernmental transfers and understanding of finances of Central and State governments. In short, the whole approach to the appointment of the Finance Commission and its functioning has not been very professional. Thus, not surprisingly, and unlike the Australian Commonwealth Grants Commission, their contribution to the development of an objective and scientific approach and methodology to satisfactorily resolve fiscal imbalances and infuse confidence to cement stronger intergovernmental relationships has left much to be desired. In the event, the very objective of establishing an independent semi-judicial body to recommend intergovernmental transfers has been defeated.

Lack of co-ordination between Planning and Finance commissions is another important issue. The whole exercise is based on the incorrect assumption that the plan and non-plan sides of the budget are independent and exclusive. Parallel assessment of State finances by the two agencies not merely results in duplicating the work; there are instances where the Planning commission has gone about filling the non-plan gaps of the States in the current account, resulting from the non-compliance of the norms set by the Finance Commissions. The States on their part, submit different projections of revenues and expenditures to the two commissions; the projection submitted to the Finance Commission attempts to magnify the gap in the revenue account in order to get larger assistance whereas, the one submitted to Planning Commission exaggerates the availability of resources to

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\(^1\) The Member-Secretaries of both the Ninth and Tenth Finance Commissions were changed mid-way through the Commissions’ deliberations as they were transferred to administrative departments.
have larger plan size. The presence of a common member in Planning and Finance commissions has resolved this issue to a considerable extent, but the issue to independent treatment of interdependent plan and non-plan sides remains.

The important issue from the above is that political elements enter into fiscal transfer decision in all federal countries. To that extent, actual transfer system deviates from the ideal either in its design or implementation. Politics matters and we do not live in the world of benevolent State. The agents - be they politicians or bureaucrats are self interested and yet, it is possible to enhance objectivity and evolve a scientific approach when the ideas of commitment and delegation discussed in chapter 4 and 5 are satisfied and the system of checks and balances is allowed to function.
Regional Policies and Invisible Transfers

(a) Redressing Inter-State Disparities: Regional Policies

In a centrally planned economy, investment planning and its regional spread is determined by the government and therefore, given the endowment of natural resources and nature of institutions, the pattern of regional growth and inter-regional distribution of incomes is largely determined according to regional policies. However, in a mixed economy the distribution of private sector investment is also important.

(i) Redistributive impact of Central public enterprises:

In India, one of important components of regional policies is the distribution of the Central Government’s own investments and the direction to credit disbursal from the commercial banks. It is difficult to draw implications on the incidence of Central Government’s budgetary spending in the absence of a detailed empirical analysis. However, the spread of central investments in various enterprises is available. Clearly, the strategy of public enterprise dominated heavy industry based development strategy directed considerable investments in mineral rich States of Bihar (including Jharkahand), Madhya Pradesh (including Chattisgarh) and Orissa during the first three five year plans. Substantial investments were also made in heavy industries and this included heavy electrical industry in Bhopal and aircraft industry in Sunabeda in Orissa in the first three plans. However, the policy of taking over of sick private manufacturing units in the subsequent Plans resulted in the spread of investments which is different from that was originally envisaged.

Despite pronouncements on balanced regional development, the spread of Central Government investment has not ensured balanced regional development. It is seen from Table 9 that low per capita income States with population share of 45 per cent accounted for only 29 per cent of the total investments in Central Government enterprises and 41 per cent of the total employment generated in central enterprises. In fact, income share of these States was equal to the investment share. Similarly the share of employment in central enterprises was lower than their population shares by 4 percentage points. In contrast, the above average income States with 49 per cent of population accounted for
58 per cent of the investments and 65 per cent of the income generated in the country. Thus, the investments in central enterprises has not attempted to bring achieve balanced regional allocation of investments. The story of Bihar is even more telling. The poorest State with about 8.2 per cent of population received only about 2 per cent of the accumulated Central Government investments until 2003-04 and these accounted for just about 1 per cent of employment in central enterprises.

Table 9
Inter-State Allocation of Investments in Central Government Enterprises – 2003-04
(Per cent of total)

<table>
<thead>
<tr>
<th></th>
<th>Population Share</th>
<th>GSDP Share</th>
<th>Investment Share</th>
<th>Employment Share</th>
</tr>
</thead>
<tbody>
<tr>
<td>Goa</td>
<td>0.14</td>
<td>0.44</td>
<td>0.07</td>
<td>0.12</td>
</tr>
<tr>
<td>Punjab</td>
<td>2.41</td>
<td>3.97</td>
<td>1.56</td>
<td>1.72</td>
</tr>
<tr>
<td>Maharashtra</td>
<td>9.57</td>
<td>15.09</td>
<td>19.38</td>
<td>12.80</td>
</tr>
<tr>
<td>Haryana</td>
<td>2.08</td>
<td>3.24</td>
<td>2.34</td>
<td>1.29</td>
</tr>
<tr>
<td>Kerala</td>
<td>3.15</td>
<td>4.09</td>
<td>2.75</td>
<td>2.77</td>
</tr>
<tr>
<td>Gujarat</td>
<td>5.00</td>
<td>6.86</td>
<td>7.04</td>
<td>3.26</td>
</tr>
<tr>
<td>Tamil Nadu</td>
<td>6.16</td>
<td>7.94</td>
<td>6.92</td>
<td>5.42</td>
</tr>
<tr>
<td>Karnataka</td>
<td>5.23</td>
<td>6.34</td>
<td>5.32</td>
<td>5.11</td>
</tr>
<tr>
<td>Andhra Pradesh</td>
<td>7.53</td>
<td>8.66</td>
<td>7.63</td>
<td>6.34</td>
</tr>
<tr>
<td>West Bengal</td>
<td>7.91</td>
<td>8.40</td>
<td>5.28</td>
<td>13.48</td>
</tr>
<tr>
<td>High Income States</td>
<td><strong>49.19</strong></td>
<td><strong>65.02</strong></td>
<td><strong>58.30</strong></td>
<td><strong>52.31</strong></td>
</tr>
<tr>
<td>Rajasthan</td>
<td>5.58</td>
<td>4.98</td>
<td>2.77</td>
<td>1.91</td>
</tr>
<tr>
<td>Chhattisgarh</td>
<td>2.05</td>
<td>1.71</td>
<td>2.17</td>
<td>6.40</td>
</tr>
<tr>
<td>Madhya Pradesh</td>
<td>5.97</td>
<td>4.67</td>
<td>4.97</td>
<td>6.77</td>
</tr>
<tr>
<td>Jharkhand</td>
<td>2.67</td>
<td>1.79</td>
<td>4.11</td>
<td>15.32</td>
</tr>
<tr>
<td>Orissa</td>
<td>3.64</td>
<td>2.42</td>
<td>5.65</td>
<td>4.18</td>
</tr>
<tr>
<td>Uttar Pradesh</td>
<td>16.42</td>
<td>10.38</td>
<td>7.18</td>
<td>5.48</td>
</tr>
<tr>
<td>Bihar</td>
<td>8.20</td>
<td>2.99</td>
<td>1.87</td>
<td>1.17</td>
</tr>
<tr>
<td>Low Income States</td>
<td><strong>44.53</strong></td>
<td><strong>28.94</strong></td>
<td><strong>28.72</strong></td>
<td><strong>41.23</strong></td>
</tr>
<tr>
<td>Arunachal Pradesh</td>
<td>0.11</td>
<td>0.11</td>
<td>0.39</td>
<td>0.12</td>
</tr>
<tr>
<td>Assam</td>
<td>2.63</td>
<td>1.89</td>
<td>4.73</td>
<td>3.26</td>
</tr>
<tr>
<td>Himachal Pradesh</td>
<td>0.60</td>
<td>0.91</td>
<td>2.93</td>
<td>0.68</td>
</tr>
<tr>
<td>Jammu and Kashmir</td>
<td>1.00</td>
<td>1.03</td>
<td>1.98</td>
<td>0.55</td>
</tr>
<tr>
<td>Manipur</td>
<td>0.23</td>
<td>0.23</td>
<td>0.04</td>
<td>0.06</td>
</tr>
<tr>
<td>Meghalaya</td>
<td>0.24</td>
<td>0.23</td>
<td>0.03</td>
<td>0.12</td>
</tr>
<tr>
<td>Mizoram</td>
<td>0.08</td>
<td>0.11</td>
<td>0.06</td>
<td>0.06</td>
</tr>
<tr>
<td>Nagaland</td>
<td>0.19</td>
<td>0.25</td>
<td>0.19</td>
<td>0.06</td>
</tr>
<tr>
<td>Sikkim</td>
<td>0.06</td>
<td>0.07</td>
<td>0.28</td>
<td>0.06</td>
</tr>
<tr>
<td>Tripura</td>
<td>0.32</td>
<td>0.39</td>
<td>0.27</td>
<td>0.12</td>
</tr>
<tr>
<td>Uttarakhand</td>
<td>0.84</td>
<td>0.83</td>
<td>2.07</td>
<td>1.35</td>
</tr>
<tr>
<td>Special Category States</td>
<td>6.28</td>
<td>6.04</td>
<td>12.98</td>
<td>6.46</td>
</tr>
</tbody>
</table>

Total: **100.00**  **100.00**  **100.00**  **100.00**

Even the investments made in the poorer regions have not had the desired impact on their regional economies. The multiplier – accelerator process that is supposed to activate developmental process from these large investments was nullified by the freight equalization policy. Under this basic raw materials such as steel and coal were made available at uniform prices throughout the country by the Central Government providing subsidy to offset freight charges. The consequence of the policy was to reduce the forward linkages from these investments besides reducing the overall productivity of investments in the country. Investments in coal and steel was basically intended to promote both backward and forward linkages and as these have a strong resource base, they had significant backward linkages to exploit their mineral resources. Although this policy has been given up, it is not possible to reverse the investment decisions that have already been made.

Table 10
Credit-Deposit Ratios in Indian States

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Tamil Nadu</td>
<td>0.94</td>
<td>0.91</td>
<td>0.91</td>
<td>0.90</td>
</tr>
<tr>
<td>Maharashtra</td>
<td>0.79</td>
<td>0.70</td>
<td>0.85</td>
<td>0.81</td>
</tr>
<tr>
<td>Andhra Pradesh</td>
<td>0.74</td>
<td>0.76</td>
<td>0.63</td>
<td>0.68</td>
</tr>
<tr>
<td>Karnataka</td>
<td>0.75</td>
<td>0.68</td>
<td>0.59</td>
<td>0.63</td>
</tr>
<tr>
<td>Rajasthan</td>
<td>0.68</td>
<td>0.46</td>
<td>0.48</td>
<td>0.57</td>
</tr>
<tr>
<td>Gujarat</td>
<td>0.58</td>
<td>0.47</td>
<td>0.49</td>
<td>1.13</td>
</tr>
<tr>
<td>Madhya Pradesh</td>
<td>0.56</td>
<td>0.53</td>
<td>0.47</td>
<td>0.48</td>
</tr>
<tr>
<td>West Bengal</td>
<td>0.60</td>
<td>0.54</td>
<td>0.44</td>
<td>0.49</td>
</tr>
<tr>
<td>Kerala</td>
<td>0.68</td>
<td>0.45</td>
<td>0.43</td>
<td>0.47</td>
</tr>
<tr>
<td>Haryana</td>
<td>0.72</td>
<td>0.47</td>
<td>0.42</td>
<td>0.48</td>
</tr>
<tr>
<td>Orissa</td>
<td>0.59</td>
<td>0.54</td>
<td>0.41</td>
<td>0.54</td>
</tr>
<tr>
<td>Punjab</td>
<td>0.43</td>
<td>0.41</td>
<td>0.41</td>
<td>0.43</td>
</tr>
<tr>
<td>Uttar Pradesh</td>
<td>0.42</td>
<td>0.35</td>
<td>0.28</td>
<td>0.33</td>
</tr>
<tr>
<td>Bihar</td>
<td>0.41</td>
<td>0.33</td>
<td>0.24</td>
<td>0.26</td>
</tr>
<tr>
<td>Average</td>
<td>0.65</td>
<td>0.58</td>
<td>0.57</td>
<td>0.63</td>
</tr>
<tr>
<td>Coeff. of Var.</td>
<td>0.22</td>
<td>0.27</td>
<td>0.32</td>
<td>0.37</td>
</tr>
<tr>
<td>Coeff. of Var. (SDP)</td>
<td>0.32</td>
<td>0.40</td>
<td>0.36</td>
<td>0.41</td>
</tr>
<tr>
<td>Corr* with per capita SDP</td>
<td>0.11</td>
<td>0.18</td>
<td>0.59</td>
<td>0.48</td>
</tr>
</tbody>
</table>

Source: RBI Bulletins, National Accounts Statistics, and Indian Census. Figures for Bihar, Madhya Pradesh and Uttar Pradesh in 2001 include Jharkand, Chhattisgarh and Uttarakhand respectively.
(ii) Redistributive impact of commercial bank functioning:

Another important initiative taken by the government of India was to expand the network of bank branches to rural areas and poorer regions, particularly after the nationalisation of the major commercial banks in 1969. However, relative density of commercial banks in poorer regions continues to be lower than in middle and high income States. Furthermore, the expansion of banking network has served to transfer household savings of poorer States for investment in more affluent States.

Table 10 shows the credit deposit ratios in the 14 major States in descending order of their ratios as seen in 2004-05. The interesting inferences drawn from the table are: (i) by and large although credit – deposit ratios although were higher in more developed States, there are important exceptions. Punjab, Haryana and Gujarat are the high income States with lower credit- deposit ratios. (ii) The credit - deposit ratios were generally higher in States with relatively more manufacturing activity. Thus, States such as Tamil Nadu and Maharashtra had much higher credit deposit ratios as compared to Punjab, Haryana, Uttar Pradesh and Bihar. The ratios in the last two States were abysmal and in part, this reflects total lack of activities taking organized sector credit in these States. (iii) The relative position has changed very little from 1980. Exception to this are the cases of Kerala, Gujarat and West Bengal, which have moved down in their rankings substantially. (iv) The ratios have shown a steady decline in every State (except Maharashtra) indicating that commercial banks, as a policy tend to employ their resources increasingly to other ways of earning their incomes including investment in government securities. The decline has been particularly sharp in the two poorest States of Bihar and Uttar Pradesh. These States have the low credit-deposit ratios and it has been showing sharp declines.

(iii) Redistributive impact of Centre’s Explicit and Implicit Subsidies:

An important way in which the Central Government can influence the regional allocation of resources is by spending directly on various services in States. The Centre has powers to spend on both social and physical infrastructure directly or can institute transfer systems for augmenting various public services. The central expenditures comprise of substantial proportion of public good type of expenditures which are supposed to benefit the entire population and these include spending on defense and general administrative services and debt service payments. However, incidence of spending on social and economic services can be traced to different States. A recent study attempts to estimate the regional incidence of explicit and implicit subsidies of the Centre (Chakraborty, Mukherjee and
In this, various implicit and explicit subsidies under social and economic services which they characterize as “quasi fiscal transfers” to States are estimated and their regional incidence worked out for 2007-08. Their estimates presented in Table 10 shows that in general, the distribution of Central subsidies among States is regressive.

The results of their econometric investigation are presented in Table 11. The results on formula based transfers from the Finance and Planning Commission conform to the analysis on carried out in the previous section. While the tax devolution and formula based transfers show a significantly progressive distribution, the non-formula transfers from the Centre to the States is not significant. In contrast, the distribution of central subsidies is significantly regressive with the states with higher per capita GSDP receiving larger per capita subsidies. The State with one per cent per capita GSDP gets 0.65 per cent higher Central subsidies. In fact, the regressive nature of these quasi fiscal transfers is so high that when they are added to the explicit central transfers, the entire transfer system becomes significantly regressive.

(b) Invisible Transfers in Indian Fiscal Federalism

The foregoing analysis demonstrates that even when there is a Constitutional mechanism to effect formula based transfers, the political system may not allow evolving a simple, equitable, objective and rule-based system of transfers as demonstrated in Indian federation. Even if such a system is developed, there can be a number of implicit and invisible ways in which political economy factors can work to effect resource transfers in unintended ways. Invisible transfers arise whenever there are controls on prices and, these impact on the regional income levels and allocation of resources. The controls could be in terms of determining the procurement price of foodgrains or administered pricing of petroleum products or below market interest rates for government borrowings.

In a transitional economy like India, there are several controls including those on prices of various commodities and interest rates. The analysis of subsidised lending to State undertaken some years ago shows that the regressivity of these subterranean or invisible transfers offset whatever progressivity the explicit transfer system had shown (Rao, 1997). Another important source of invisible transfers is the inter-State tax exportation. The levy of central sales tax by the exporting state converts the sales tax into a origin based tax and passes on a significant proportion of tax burden from more affluent producing states to the consumers in poorer consuming states. Although there are no statistics measuring the inter-state trade, there is enough anecdotal information to show that inter-
state tax exportation can be significant in Indian context. There are also a variety of other sources of inter-State resource transfers due to Central policies and these include subsidised borrowing by the States from the Central Government and the banking system, subsidised lending by banking and financial institutions to the private sector, subsidised finance provided to refinancing institutions such as Infrastructure Development and Finance Company Ltd. (IDFCL) at below market interest rates, loan waiver effected by the Central Government in which the Central Government subsidises the commercial and co-operative banks for waiving the loans of the farmers as well as priority sector lending by commercial banks for specified activities like agriculture and rural development, industrial promotion, small scale industry and exports.

Unfortunately, these subterranean transfers have not been systematically estimated. However, as mentioned earlier, anecdotal evidence in respect of some of these invisible transfers shows that such transfers can be significant. Therefore, even as the transfer system attempts provide larger resources to poorer states to enable them to provide better standards of infrastructure, these subterranean transfers tend to create much more competitive inequality in Indian federation.
Reforming Intergovernmental Finance in Indian Fiscal Federalism

The foregoing critical review of Indian fiscal federalism underlines the need to undertake reforms in several areas. The reforms are needed both in the policies and institutions to make Indian fiscal federalism to respond more effectively to the requirements of liberalised, outward oriented market economy. Although the existing multilevel fiscal system has provided the institutional support for over 60 years in terms of providing a reasonably stable governance system, it can not be stated with confidence that it has satisfactorily resolved the difficulties arising from religious, linguistic, ethnic and cultural diversities. Even more important, there is considerable dissatisfaction with delivery of public services including basic security and safety to the population which is an essential pre-requisite for savings, investment and economic growth (Olson, 1991). In a competitive international environment, in addition to providing a secure business environment, it is necessary to provide efficient standards of social and physical infrastructures on the one hand and finance these services through taxes which are least distorting.

This foregoing analysis undertakes a critical examination of both policies and institutions relating to Indian multilevel fiscal system. It analyses the assignment system, and overlapping in the assignments, the policies and institutions to deal with fiscal imbalances with a view to identifying areas requiring reforms. The analysis is undertaken taken into account the norms given by the theories of fiscal federalism and the best practices in conducting intergovernmental fiscal relationships in other federations.

(a) Some Implementable Rules.

The first and second generation theories of fiscal provide important rules for efficient system of fiscal federalism. They help in identifying the factors determining the success of fiscal federalism in terms of providing an institutional framework for public service delivery which is essential for achieving economic prosperity and reducing poverty while retaining individual identities and receiving the public services closely matching the diversified preferences. The important features identified for a successful fiscal federalism are:
(i) Efficient public service delivery requires unambiguous assignment system. Clarity in assignments is akin to providing clear property rights which provides a necessary environment for both incentives and accountability.

(ii) The assignment system, to be efficient, should be according to comparative advantage. The efficient degree of decentralisation is determined by the extent of diversity in preferences, the provision including transaction cost of providing various public services which inter alia, depends on the state of technology and the possibility of productivity gain through innovation due to efficient intergovernmental competition.

(iii) Gains from fiscal federalism can be realised only when the system enables provision of services according to diversified preferences while taking advantage of the large common market. For realising the latter, it is necessary to remove all impediments and facilitate mobility and trade in commodities as well as factors of production across the country to make truly a customs union.

(iv) In order to reap gains from intergovernmental competition, it is necessary to have a system to prevent predatory competition which inter alia, requires ensuring a measure of competitive equality through equalizing regional policies, intergovernmental transfers and prevention of various sources of invisible transfers.

(v) The transfer system while achieving a equalization should not provide incentive to fiscal profligacy and laxity. It is important to checks against competition to pass on the burden of financing public services in a state to the non-residents. Sixth, the subnational governments should have hard budget constraints. Bail outs soften the budget constraints, create perverse structure of incentives against following a prudent, growth oriented economic policies and encourage fiscally irresponsible behaviour.

Much of the mainstream literature on fiscal federalism is based on the premise of market economy, and these need to be modified to the situations in developing and transitional economies. The norms have to be modified to the cases where the predominant traditional sector links poorly with markets, segmented labor markets, low level of savings and investment with a large part of the savings in physical rather than financial assets, imperfect market for land, imperfect mobility of labour, capital and commodities. In a planned economy, there are controls on prices and outputs and these alter inter-regional resource
allocations in unintended ways. The invisible transfers created from these polices create their own dynamics and the explicit transfer system, ignoring these may not be able to achieve intended results.

(b) Major Reform Issues in Indian Fiscal Federalism:

Historical factors have contrived to impart a high degree of centripetal bias into Indian Constitution. Although the Cabinet Mission that visited India before independence recommended a highly decentralized federal system. However, once the Muslim majority regions separated to form a separate country – Pakistan and as some of the Princely States started asserting their rights to create a fissiparous environment, the founding fathers drafted the Constitution that is highly centralised. In fact, the Constitution describes India as a “Union of States”, and nowhere in the Constitution, the term “federalism” is used to describe the polity.

In fact, the centralizing features of the Constitution have led many a scholar to state that India is a “quasi-federal” country. The Constitution relies heavily on and follows closely the Government of India Act, 1935. While this did serve the purpose of stabilizing the polity in the formative years, and did not pose serious constraints when the economy followed the inward looking development strategy, it is unresponsive to the requirements of a liberalized and globalising economy. The centralization inherent in the Constitution was reinforced with the adoption of planned development strategy which made the States in the Indian Union subservient to the Central Government in determining the development approach and allocation of resources. Continued intrusion and excessive centralization has not allowed the country to realise the beneficial effects of decentralisation fully. It has not provided appropriate environment for the state and local governments to compete with one another and innovate in and has helped to realise the potential gains from decentralisation fully.

Although symmetry in the status and power among subnational territorial units is a norm in federations, some formal asymmetry has always been present even in the most classical federations (Bird, Bird and Ebel, 2007). As argued by Riker (1964), federalism is a bargain among politicians and the terms of accession depend on the bargaining strength. It is therefore not surprising that there is significant asymmetry in Indian federalism as well. The paper discusses the asymmetric arrangements in Indian federation particularly in respect of Jammu and Kashmir, and Northeastern States. While these are rule based asymmetries that go to cement and strengthen rather than weaken the federation, the
asymmetric implementation of policies for political reasons can impart disaffection and instability to Indian fiscal federalism. This underlines the need to strengthen the rules as well as institutions of intergovernmental finance in Indian fiscal federalism.

The dominance of single party rule at both Central and State levels, committed leadership, who were in the forefront of independence movement at the helm of national affairs and the unflinching faith in the leadership of the national leaders helped to resolve all contentious inter-State and Centre – State matters in an informal environment. The informal system of conducting intergovernmental relationships has impeded the development of both rules and institutions to conduct and strengthen intergovernmental relationships and resolve inter-State and Centre-State disputes. The glaring case of inadequacy of rules of institutional vacuum is in the inability to resolve river water disputes among the states.

The informal system of intergovernmental relations, as mentioned above has created an institutional vacuum in Indian fiscal federalism. There are no credible and effective institutions to undertake intergovernmental bargains and resolving disputes. The creation of Inter-State Council based on the recommendations of Sarkaria Commission has not filled the void; as a part of the Union Home Ministry, it can not be an impartial arbiter. Nor has it been empowered to undertake such a task and the experience shows that it has not been very effective in dealing with even the inter-state issues. The NDC has been a formal Organisation without much operational significance and is not designed to deal with day to day issues of intergovernmental relationships. Rajya Sabha, the upper house representing the States in the Parliament is supposed to safeguard the interests of the States in the Parliament, but effectively it does not represent the States nor does it safeguard its interests as voting in the Parliament is done essentially on party lines. Institutions like Empowered Committee of State Finance Ministers has helped to forge a united front of the states to bargain with the Centre in regard to the introduction of VAT and goods and services tax (GST). While this has been useful in effectively bargaining and negotiating with the Centre in safeguarding the interest of the States, the arrangement is purely ad hoc. It does not have a statutory position and has not been effective even in resolving matters related to the departures from the consensus agreements arrived at in the meetings. The lack of institutions and the system to conduct intergovernmental relationships and provide an effective mechanism for bargaining and resolution of conflicts is a major shortcoming in Indian fiscal federalism. Such an institution is extremely important for ensuring a harmonious working of fiscal federalism in India.
An important advantage of a federation is that while it serves to cater to the diversified preferences in different regions and ensures their regional identities, it helps to reap the advantages of a unified common market and reap scale economies in production process. This is important to enhance competitiveness and in a globalising environment, ensuring unfettered factor and product markets nation-wide is essential. The linguistic diversity in itself is a major impediment to the movement of labour. In addition, the system has provided incentive for partisan approaches such as reservation of jobs for the locals, movements against the use of languages other than the local language. The system of restricting the movement of essential commodities and rationing introduced in the initial years after independence due to acute scarcity conditions have continued even as the scarcity conditions have eased. Besides Essential Commodities Act, there are restrictions land as Urban Land Ceiling Act and Rent Control Act, which were ostensibly enacted to protect the interests of the disadvantaged, but have ended up as factors impeding the nation-wide market and enabling facilitating urban rural migration of population. In addition there are various other tax and other regulatory impediments such as the central sales tax which is a tax on the exports from one state to another, and Octroi, which is a tax on the imports into a local body and these have divided the country into several tariff zones. These, violate a basic principle of fiscal federalism and other protectionist policies which are inimical to the competitiveness of the country.

There are several problems with the functioning of Indian fiscal federalism. The assignment system has a considerable degree of ambiguity. In the case of the tax assignments, the principle of separation of taxes followed in the Constitution has not helped to prevent tax disharmony. It would be advisable to enable concurrent taxation of personal income taxation with the Centre determining the tax base and States as well as the local governments piggybacking their levies on that base and the tax room for each of the three levels can be determined by negotiation. Similarly, in the case of consumption taxes, the levy of GST will do away with considerable problems of disharmony that prevails at present and even in this case, the local governments too can be allowed to piggyback on the tax levied by the States subject to a ceiling rate. This would provide significant resources for the local governments that are starved at present and that can improve the service delivery.

Assignment system in the case of expenditures has significant overlapping and the consequences have been to adversely impact on the quality of public services delivered and accountability. As mentioned earlier, excessive centralization does not promote the
markets and does not enable the governmental units to compete with one another in a manner that is beneficial to the economy. It is therefore, necessary to go back to the drawing board and rework the assignment system based in comparative advantage. It is also important to note that there have been several areas in which the Centre has intruded into the legislative domains of the States mainly for political reasons. Similar approach is seen by the States encroaching on legitimate domains of local bodies. Another mechanism is to institute a specific purpose grant and channel it directly to the implementing agencies bypassing the States. Many of these schemes involve matching contributions by the State governments. Thus, while the Centre wants to claim ownership to these schemes, it wants to alter the pattern of allocation of expenditures by the States. The most important and of course, difficult task is to rework the system to ensure clarity in the roles of Centre, States as well as local governments.

The Constitution recognises that the assignment system results in significant vertical fiscal imbalance. It also recognises that history, institutions (including the standards of governance) and resources have contrived to create significant differences in infrastructure, market access and development among different States resulting in significant levels of horizontal imbalances. Therefore, it provides for Articles 270 and 275 for transferring resources from the Centre to the States to enable the states to provide comparable levels of public services even when they raise revenues at comparable tax efforts. To ensure that this is done in an objective manner, the Constitution provides for the appointment of the Finance Commission under Article 280. Despite this, the transfer system that has been evolved in the country has not served the purpose satisfactorily resolving the issues either vertical or horizontal imbalance.

A major issue in Indian fiscal federalism relates to the multiple agencies giving transfers. Although in the Constitutional scheme of things, the Finance Commission is supposed to be the sole agency. The emergence of Planning Commission and various Central ministries as major dispensers of central assistance relegates the Finance Commission to a minor role. This has led to several developments. First, there are serious questions of legitimacy of giving transfers through the mechanism outside that is mandated in the Constitution. Second, discretionary transfers in which, political economy considerations are important have taken a precedence over statutory transfers making the system of transfers less objective and impartial. Third, no agency takes a holistic view of the requirements of the States for various services and the resources can be raised by each state with normatively given revenue raising effort and in the process, is
not able to design and implement a holistic plan of equalization. Finally, given that political economy considerations predominate in the design and implementation of discretionary, particularly non-formulaic transfers, neither the objectives of offsetting horizontal and vertical fiscal imbalances nor ensuring minimum standards in respect of basic services that are considered meritorious through the transfer system have been realised.

The empirical analysis of various transfers substantiates the above conclusion. The analysis shows that the transfer system as a whole has failed to offset the fiscal disabilities of the poorer states. In the event, the per capita development expenditures in the States have a significant positive correlation with per capita GSDP and naturally, this has led to significant inter-State inequalities in social and physical infrastructures. These have created inequalities in the competitive strength of the states.

There are serious questions of legitimacy of giving grants under Article 282 of the Constitution. Eminent jurists like Mr. K. K. Venugopal and A. G. Noorani are of the view that giving grants under Article 282 is unconstitutional. Mr. Venugopal arrives at this conclusion first, on the positive interpretation of Article 275 and second on the detailed analysis of the non-obstante clause in Article 282. The reading of the Article 275 shows that all grants, be it general or specific purpose, conditional or unconditional or for capital or revenue purposes can be given under Article 275. The non-obstante clause of Article 282 states, “notwithstanding that the purpose is not one with respect to which Parliament or the legislature of the State, as the case may be, may make laws” which implies that this is not merely meant to lift the bar for both the States and the Centre to make grants for any public purpose to institutions on subjects beyond their legislative purview as listed in the Union and State lists. This can not be a miscellaneous provision because it visualises that the grantors could either be the Union or a State. In his view, “…to the extent that any of the terms of reference seek to deprive the Finance Commission of its powers which are constitutionally vested in it under Article 280, Clause 3, the terms would be invalid and unconstitutional” (NIPFP, 1993; p. 274).

In this scenario, how should the institutional reforms in regard to Planning and Finance Commissions be addressed? One way would be to clearly delineate the responsibilities of the two institutions. The Planning Commission could be entrusted with the task of assessing infrastructure requirements and draw up a plan for its implementation including the plan of financing it. As the practice of Central Government giving loans to States has
been given up based on the recommendations of the Twelfth Finance Commission, the financing of infrastructure has to be done predominantly through market borrowing or borrowing from the National Small Savings Fund. All grants should be given on the basis of the recommendations by the Finance Commission. There are however, questions about the ability of the Finance Commission to monitor the implementation of recommendations which is considered to be an ad hoc and a temporary body. A clear reading of Article 280 shows that there is nothing in the Constitution to make it either *ad hoc* or temporary. The Article reads, “The President shall, within two years of the commencement of the Constitution appoint a Finance Commission and thereafter every five years or earlier . . .” Indeed, the Finance Commission can be appointed for a period of five years and on the expiry, a new Finance Commission can be appointed. It should be supported by a strong secretariat with well qualified scholars appointed to undertake continuous research and monitor the implementation of its recommendations. It can give all grants, capital as well as revenue and block grants as well as conditional. In fact, in order to ensure some basic standards of physical infrastructure, the Commission may recommend capital grants if it thinks necessary. It can monitor the entire gamut of central sector and centrally sponsored schemes to impart accountability.

An important part of making Indian fiscal federalism competitive is the reform of fiscal relationship between the States and local governments. There is much that is wrong with sub-state fiscal decentralisation. While in China, the local governments have proved to be catalysts in the developmental process and in particular, intergovernmental competition has been a major factor in making innovations, accelerating growth and expanding exports, in India despite the Constitutional recognition, they have continued to be dormant and have not played their potential in the developmental process of the country. In fact, the problems begins with ambiguity and overlap in the assignment system. The areas earmarked to rural and urban local governments in Schedule 11 and 12 of the Constitution have to be concurrently carried out by them with the States and the nature and extent of devolution is determined at the State’s discretion. At the initiative of the Ministry of Panchayati Raj, many States undertook activity mapping, but this was more a ritualistic exercise and the ambiguity in assignments have continued.

The design of decentralisation is just not in keeping with the implementable rules of fiscal decentralisation (Bahl, 2002). The assignment system is unclear. The local governments do not have revenue handles to vary the public services according to the preferences of the residents. Obviously, the there is not way to match revenue – expenditure
decisions even at the margin to ensure incentives and accountability. There is no system of devolving functions, finances and functionaries in a coordinated manner. The transfer system is unstable and ad hoc and is not based on the requirements of the local governments to enable them to provide public services devolved to them in any satisfactory manner. There is virtually no reliable information system to enable proper planning and implementation of public service delivery.

Ironically, the local governments have not been able to undertake the functions assigned to them in any satisfactory manner. First of all, they do not have adequate revenue handles to finance the public services they are required to provide. Secondly, they are not able to raise revenues even from the revenue handles assigned to them in any satisfactory manner due to poor capacity to collect revenues. Nor is there any satisfactory system of providing systematic and regular grants to them. The States have been irregular in appointing the State Finance Commissions. The Commissions do not have the capacity to undertake the task of assessing the requirements of the local governments in any systematic manner. The recommendations made by the Commissions are often not implemented partly because the most of the recommendations are not implementable. Ion the whole the issue of assessing the expenditure requirements of the local governments for the functions devolved to them is not done in any systematic manner. The grants given by the State governments are ad hoc, often scheme based and even when block grants are given, deduction of electricity bill at the source takes away significant proportion of the grants given. The consequence of all these is that the standards of local public services delivered is abysmal. Reform of the local government fiscal system is another important component of the reform of Indian fiscal federalism.
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Independent Budgeting and Planning at District Level

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We are presenting here our draft report of the study which requires much further improvement. However, we are grateful to all the above once again that we are given this opportunity. We have attempted to the best of our ability to incorporate the earlier comments provided by the authorities of the Commission. We are thankful to them and we expect their kind cooperation regarding the same.
Executive Summary

The constitution provides the status of local self-government for the local bodies. The constitutional status means that the local governments are on par with the Central and State governments. In the Constitutional status of local self-governments they, can plan for their economic and human development. This fact however is undermined in practice at the state level. The provision provided in the 74\(^{th}\) Amendment Act for creating and activating District Planning Committee is the responsibility of the state governments. This often is also in contradiction with the interests of the real politik of the state level governments. Often DPCs are not constituted, if constituted they are dysfunctional. The creation of institutions for local level independent planning and budgeting itself is a political process fraught with many a quagmire. The hurdles are not only political but bureaucratic as well.

The above statement comes out of this study of Tumkur district in Karnataka. Karnataka is traditionally known as a state which championed decentralisation process. The state had seen number of experiments in decentralisation. The most important of them was to strengthen the Zilla Panchayats with all the development functions devolved to them and a bureaucrat senior in rank to the Deputy Commissioner (collector) being appointed as the ‘Chief Secretary’ to the elected representatives of the Zilla Panchayat. And also provision of 25 percent of reservation for women in Panchayats much before the positive discrimination was announced through parliamentary Acts. Karnataka is usually considered therefore as a progressive state so far as the decentralisation process is concerned.

The above arguments are often elevated to the status that the progressive and successful decentralisation is one of the two pillars of the ‘Karnataka Model’ of development; the other being the advanced information and biotechnology led economic development process. The Karnataka Model therefore is said to be ideal and suitable for other states as well. There is considerable truth in this. And there is considerable fog around the truth as well. The fact is that in the DPCs are not even constituted in all districts. In Tumkur, where we conducted our study the DPC was constituted in 2007-2008 but it has not held single meeting so far. Therefore the Model of Karnataka is useful but rests on feet of clay.
In order to understand the situation we have to consider that fact that there are at least three factors that this study brings to bold relief, they are: a) the devolution process; b) the integration process and c) the implementation process.

**Devolution Process:**

It comes out clearly from the study that the devolution of funds, functionaries and functions is only partial in Karnataka. The Karnataka Panchayati Raj Act and subsequent official pronouncements hold that all the 29 items in the 11th Schedule of the Constitution are devolved to the PRIs. This is only partially true. One study shows that only 14 items out of the 29 items are devolved to Gram Panchayats in the state (Rajasekhar and Satpathy, 2007). However this is considerable compared to other Indian states. Our study shows that there is considerable devolution of funds and finances to the lower tiers and particularly to the Gram Panchayats. Every Gram Panchayat at the time of the study received, according to their population and other criteria, from 25 to 40 lakh rupees from the state and central level governments. In addition to these there is a specific World Bank scheme going on in the state which provides untied grants every year to Gram Panchayats from six to ten lakh Rupees. Therefore there is sufficient devolution of funds in the state to the lower most tier of the Panchayati Raj system.

The study findings show that most difficult and inadequate part of the devolution in Karnataka is the devolution of functionaries. The staff for most of the functions in general and for budgeting and planning in particular is working on deputation from other departments which have nothing to do with either budgeting or planning. They are usually from animal husbandry, horticulture, sericulture or at best rural development departments. And these planning functionaries scarcely know anything about planning the funds and functions that are available. Therefore this study clearly notes that while there is considerable devolution of funds and functions, the question of functionaries is a major problem. This study holds that there should be a separate cadre of functionaries in planning who are trained in conducting planning and budgeting at the level of Gram Panchayat, Taluka Panchayat and Zilla Panchayat. There is Chief Planning Officer at the District level, Taluka Planning Officer at Taluka level and at the village level it is the village secretary who helps in planning. But the functionaries at Taluka and Zilla levels are working only on deputation from some other department.
Therefore it comes out from our study that so far as the district level planning and budgeting goes there is no trained cadre to perform that function. ISEC and some other institutions are now building capacities of the existing functionaries to prepare plans. Therefore so far as the devolution process is concerned there is considerable amount of finances devolved to local bodies, there are considerable amount of functions devolved but not functionaries. Certainly the functionaries responsible for planning do not exist with sufficient capacities and numbers to utilize the funds that are available. This is some times leading to pilferage and corruption.

Integration Process

The study shows that preparing an integrated plan is a difficult task and is not taking place in an ideal manner. There are two kinds of integration processes involved. One, the integration of various development schemes and programmes into one single integrated plan; and second, integration of urban and rural plans. Both are problematic. Firstly there is no integration of plans at the Gram Panchayat level. The integration takes place at the Taluka level or at the district level. The Gram Panchayats plan and allocate budgets scheme wise and as mentioned above there is paucity at this level of know how to prepare integrated plan. The integrated plans are prepared even for longer term, say for five years, are prepared at Taluka and district levels. Village secretaries who help elected representatives in planning are not trained to perform that function.

The second major problem is that of integration of plans and budgets of rural and urban areas. This is missing. The rural plans and budgets are prepared by the different tiers of PRIs. The urban plans are prepared by the section on urban planning at the Deputy Commissioner’s office. Both are separate in planning and implementation. This total separation of urban and rural plans is conspicuous feature of district planning and budgeting. Often Taluka towns are trading, commercial towns and the Taluka Panchayat office is also physically located at the Taluka town. But the plan for Taluka town is prepared by municipal council of the Taluka town and sent to the Deputy Commissioner’s office; whereas the Taluka rural plan is sent to the Zilla Panchayat. There is need badly for the integration of both of these at the Taluka levels and district levels. This integration will help mobilize more resources for Taluka and District levels as well.

At Zilla level also there is no effort at integration of rural and urban plans. These different plans are supposed to be submitted to the DPC and the DPC is supposed to
perform the function of plan integration. Since DPC is non-functional the planning process and budgeting process at the district level operates separately for both rural and urban areas.

**Implementation Process**

This study shows that the planning and budgeting process is taken more seriously at the Gram Panchayat level that at the Taluka and Zilla Panchayat levels. This is the good practice that this study brings out. At the Gram Panchayat level, in this district, planning starts at the ward sabha level and is finalized at the Gram Sabha level. Following the above two processes the general body of the Gram Panchayat only gives its final approval. The Gram Panchayat has no powers to change the plan once it is approved by the Gram Sabha. This is a good practice emerging out of our study. While certainly the Gram Panchayat elite and the Gram Panchayat Secretary matter a great deal in this process; the local citizenry too are awake and participate in the Gram Sabha meetings.

Our study also shows that we can not idealize the above situation too much. The women ward members from SC and ST communities have said that the planning process at the village level is not inclusive. The women ward members claimed that some times the dominant caste male elite take all decisions regarding planning and budgeting. There is also the usual problem of male members of the elected representative’s family representing the female members in the Gram Sabha. Therefore while we cannot over emphasize this problem, the problem of social and political exclusion still exists. This was particularly reported from the Kunegal Taluka of Tumkur which is one of the most backward districts of the district.

Despite the above problem the local citizens in Gubbi Taluka have reported that it is the Gram Sabha which finalizes all plans budgets and beneficiaries. The case studies in Gubbi Taluka have repeatedly shown that the local citizens actively participate in the deliberations of Gram Sabha. Some Gram Panchayats in Kunegal Taluka have also reported the same claiming that the Gram Sabha is the ‘toughest exam’ for them to pass.

Therefore the implementation process for planning and budgeting is relatively transparent and accountable. This is particularly so with the World Bank aided ‘Gram
Swaraj’ plan where utmost care is taken to ensure accountability and transparency in the implementation process of plans. The Gram Swaraj plans start from ward Sabha level and are finalized in the Gram Sabha. The Gram Panchayat only formally finalizes the plans and has no power to change the plan approved by Gram Sabha; and then the plan is directly sent to the state level secretariat through the Taluka Panchayat without in anyway involving the Zilla Panchayat. This plan is for five years from 2006-07 to 2010-11 and appears to be functioning reasonably satisfactorily.

There are guidelines prepared for planning and budgeting both by the state government in Kannada language for statutory planning as well as for ‘Gram Swaraj’ planning. These guidelines are followed by the Taluka Panchayat while finalizing the plans. But these are not enough to ensure capacity building for the elected representatives and bureaucrats at the Gram Panchayat and Taluka Panchayat levels.

We have earlier mentioned about the devolution of the functionaries. One fact which we would like to bring to light is that the District level offices appeared to have less staff for planning than the Taluka level offices. The importance given to planning and budgeting appears to increase as we go down the tiers of the Panchayat system, which however is not so the case with the municipal councils.

In this executive summary we have noted the salient features of the planning and budgeting processes in Tumkur District in Karnataka. According to our study devolution of functionaries appeared a problem. Scheme wise integration is a problem at local level. Urban and rural integration of plans too is an area where we found there is a great deal to be done.


CHAPTER -1

Introduction:

The 73rd and the 74th Constitutional Amendments have brought in qualitative change in the governance of the rural and urban local bodies. The significance of these amendments is that they have established the third tier of governance as a constitutionally mandated level of governance on par with central and state governments. Local government being a state subject the state governments were asked to amend their laws to conform to the Constitutional (Amendment) Acts of 1992. Almost all the state governments have amended their laws in conformity with the parliamentary amendments.

But the fact that the local government falls under the state list has led to problems. While the central government has expected the state governments to implement the conformity laws in letter and spirit, the state governments have lacked the same. Even in best of the circumstances, the question of devolution of powers, the powers to levy taxes, the question of implementation of central schemes and the constitution and working of DPCs—District Planning Committees-- has remained a problem. The state governments even in progressive states like Karnataka have lacked sufficient enthusiasm to implement the constitutional amendments in their true letter and spirit. The situation in Karnataka and Kerala is of course far better than in the other states. But still much remains to be desired in respect of a) devolution; b) implementation of fiscal measures such as taxation, c) the implementation of central schemes; d) the question of parallel bodies and, e) the question of district planning with focus on spatial integration of the plans. This study intends to explore these aspects.

This study intends to probe into the relationship between the centre, the state and local governments with a view to evolve institutional mechanisms for preparing independent budgeting and planning at the district level. The central government has been encouraging the state governments to devolve functions, functionaries and finances to lower level bodies. The state governments have been making their efforts in this direction and local governments have been responding to these efforts; given the process what is lacking is effectiveness at the local level.
Planning process in India is done at the level of planning commission and the states and local governments adopt those plans. While this is the general situation, the 74th Amendment also makes out a case for district level planning. This is envisaged to promote planning from the level of district upwards. This process of planning from below, barring with the people’s plan experience of Kerala, is yet to take off in full fledged manner in all the states. If planning and budgeting are done in systematic manner at district level, independently and comprehensively, the development processes at the local level will be smoother. This will also make it possible to put together state level plans in realistic and meaningful manner. The priorities of local governments and state governments will become clearer and this will lead to harmonious relationships between centre-state relations on the one hand and between the local governments and the state governments on the other. Therefore the need of independent budgeting and planning at district level is obvious.

As we mentioned above, the main problem with the budgeting and planning at the district level is effectiveness. This is particularly true with planning and budgeting where the planning process is located in the DPC (District Planning Committee) in the urban areas—often at the district head quarters—going by the 74th Amendment, whereas planning is to be done for many villages in a district spanning over vast geographical areas. Besides this logistical problem, there are many procedural and processual problems in planning and budgeting at the district level. Therefore these become important and urgent areas for concern.

**Research Scope**

**Thematic Scope**—Given the above situation, the main thematic scope for research herein would be to investigate into the nature and difficulties in the processes of planning and budgeting at local and district level. This would in turn require us to look at what is the extent of devolution carried out at the state and district levels given the normative scaffolding provided by the state government. The scope of research would also involve the question of local resources. Do district and local governments have sufficient resources to plan for their priorities on their own? If not, how to augment them. The Constitution after the amendments provides fiscal and taxation powers only to the last tier of local governments i.e., the Village Panchayats, whereas the taluk and district level governments do not have provision for independent
taxation. This makes resource mobilization difficult at a level where in practice there is tremendous potential to augment taxes.

- Firstly, the scope of the study involves the question of how the schemes and programmes that are directly given to Panchayats from the centre are to be more effectively utilized; this raises the question of whether there should be tied funding from the centre or untied grants to the Panchayats. The study will examine the question of flow of funds either directly from the centre to the local bodies or routed via the State governments. This aspect has crucial repercussions to the relations between the local bodies and the State government and the relations between State government and Central government.

- Secondly, the thematic scope involves decentralized planning at the district level. As we noted above there are many a problem involved in district planning and budgeting as we will see and we take up this question squarely and examine whether there should be a single body of planning for urban and rural areas at the district level or is it more conducive to effective planning and budgeting to have a separate planning body for rural areas and for urban areas. This is the area where we intend to focus on futuristic analysis as to given the experience of planning and budgeting at the district level how best we can improve upon it. This is to be done in such a manner that the relationships between the three tiers of central, state and local governments are harmonious, smooth and their functioning effective for development.

- Thirdly, thematic scope of the study would be to explore how the relationships between the centre-state-local body relations vertically can be made harmonious and smooth and how this is to be achieved through horizontally across different districts at the state level.

- Fourthly, the study will also cover the process of dispute resolution, if any, between the state government and the local bodies at urban and rural locales. This is particularly with reference to preparation and implementation of the
budgeting and planning process. There is usually the practice of including the MLAs and MPs at the district level in the DPC but this study will examine what are all the problem areas and which need to be sorted out.

- Fifthly, the most important questions raised by the questionnaire of the Commission on Centre- State relations pertain to a) the parallel bodies to Panchayats and municipalities and b) the question of spatial planning at the district level. We approach these questions in the following manner:

- The question of parallel bodies to local bodies is a major question in all the states. In Karnataka the major parallel bodies are the *Jala Samvardhana Yojana Sanghas*, village forest committees, School Development and Monitoring Committees (SDMCs) and Watershed User’s Associations, Watershed development committees. Although, of late, attempt has been made to bring SDMCs under the jurisdiction of Panchayats at GP level, they still happen to be important parallel bodies. There are at least two problems involved here: one, the parallel bodies take away functions which ought to actually come under Panchayats. Second, the parallel bodies command more financial resources than GPs. These questions will be addressed in our study. The parallel bodies are also known in the literature as CBOs: Community Based Organizations; and as such they have their own clientele at the GP level. They also are specific and issue oriented bodies. Therefore it is argued, that they are useful. There is some truth in this.

- Our approach in the study will be to examine what are these parallel bodies, what role and scope they have, and how they can be brought under the umbrella of Panchayats. The functions related to education, drinking water, minor irrigation, natural resources conservation etc are mandated to the Constitutional bodies in the 11th Schedule of the 73rd Amendment. These functions and the funds and personnel relating to them can not be taken away from the GPs. These parallel bodies can be integrated into the Panchayats. Our attempt in the study would be to see how these can be integrated into the fold of the Panchayats and what effort can be done to incorporate the concerns of the parallel bodies into that of PRIs. This involves the study of the functions,
finances and functionaries of the existing parallel bodies as well as that of PRIs and how they can be made part of the governance and powers of the local bodies.

- The sixth question is that of spatial integration of the plans. This will be studied as to how the process is working now, and what improvements can be made regarding the process. In our understanding the process should be as follows:

- GP level plans should be prepared by taking the inventory of local resources and local priorities. These plans at the GP level should be prepared first starting from the ward level. The process should actively involve ward level all citizens as well as ward members.
- The GP level plans should be discussed in the Grama Sabha and verified with the members of the GP. Then only these plans should be forwarded to the TP.
- TP needs to integrate the plans of all the GPs in its jurisdiction and prepare a consolidated plan for the Taluk, using the inventory of resources available and prioritized needs.
- The TP then should have a meeting of all the TP members with whom the plans should be discussed; following which the TP should forward the consolidated plan to the ZP.
- The ZP then integrates all the plans into a district plan and submits it to the DPC. Here the plan that is submitted to DPC should include both the vertical dimension of the plans and the horizontal dimension of the plans. Vertically the plans start from ward levels of GPs to the ZPs. Horizontally the plans cover various PR plans as well as the municipal/urban plans.
- There are two important aspects to the above process. First is that at every stage of this planning there should be complete participation of the members of PRIs. Secondly, the process should address the rural and urban linkages squarely.
- Presently the taxation powers are vested only with GPs and not with TPs and ZPs. But TPs and ZPs are also areas where the potential of augmentation of resources is high. Therefore the planning process, while taking the inventory
of resources must identify areas where taxes can be levied and resources mobilized.

- Seventhly, the question of rural-urban linkages would be addressed squarely. Rural areas happen to spread out across vast geographical places and contain less financial resources. Urban areas are more compact, though rapidly growing areas. Towns and districts also happen to be market areas for rural citizens. Most of the commercial activities are concentrated in urban towns and municipalities. These generate urban and rural linkages. While for some districts the linkages are intensive, for some districts these linkages may be less intensive. Therefore, the ZP while recommending a district plan to the DPC should take these aspects into account and a realistic plan for each district reflecting the rural-urban linkages should be prepared for action.

- Eighthly, this study will also throw light on the proper institutions that can monitor and evaluate the planning and budgeting process. This mechanism is missing at present and since planning at the district level has not emerged in a big way the lacuna persists. In the case of planning at the district level becoming a regular exercise there is need to have in place an institution to monitor and evaluate the implementation process as well as proper systems to do so.

- Lastly, the study will examine the role that the rural local bodies can play in the acquisition of land and establishment of industrial centers in the form of Special Economic Zones. The study will take into cognizance various stakeholders at the local level and how they can be brought together in settlement process for peaceful land acquisition for cooperative and positive economic development.

Geographical Scope—The geographical scope of the study that we intend to take is one district in Karnataka where we examine whether the district level planning is being done in effective manner. Given the constraint of time this would help us to concentrate on how best to explore the present problems and future problems of district level budgeting and planning. This will be done taking all the lower tiers of local government in to purview.
**Objectives of the Study:**

1. To undertake a situational analysis of decentralized budgeting and planning at district level, by studying a district in Karnataka and providing policy recommendations for replicability of which ever the best practices evolving from the same.

2. To identify the constraints coming in the way of making the local bodies effective units of local self-governments.

3. As part of the above, to study the process of devolution of functions, finances and functionaries to different levels of local bodies and to study inter-governmental relations between the state government and local bodies as well as central-state relations.

4. In and through above to suggest if any new constitutional amendments are to be made; or to see whether major procedural changes in the existing laws would be sufficient.

**Research Questions**

The main research questions of the study will be:

- What is the extent of devolution from the state level to the district and lower tiers of government not only in terms of GOs, ordinances, documents but in terms of effective processes?

- What are the problems of devolution from the point of view of bureaucracy and from the point of view of political executive at different tiers, down from state level?
• What is the nature of fiscal devolution: what are the current problems with finances at district and lower level local bodies? How the district and local bodies are placed *vis-à-vis* augmenting resources and expending them.

• How the central schemes and programmes are implemented and what are the major difficulties involved in administering them. What are the roles of the bureaucracy and political executive in implementing and in what better ways they can be implemented. Related question is also, which are the parallel bodies to the local bodies are and how they can be brought under constitutionally mandated local bodies.

• What is the practice of district level budgeting and planning at present how best can it be improved? Can rural and urban plans be under one umbrella plan? What are the roles of political executive and bureaucracy in conducting these exercises? How to improve planning and budgeting in terms of transparency, and accountability? We would also explore whether gender and social audit of these district-level budgeting and planning processes possible. We will attempt to throw comprehensive light on the district level planning and budgeting.

• Finally how spatial integration of rural and urban plans can be done. What are the presently existing linkages between rural and urban areas, and how rural and urban plans can be prepared and integrated into a single district plan?

**Methodology**

1. The study would be based on both qualitative data generated from interviews, focus group discussions; and the quantitative data collected from the district, taluk and panchayats levels. The secondary data available from the offices of different tiers will also be incorporated. The secondary information will also be collected from documents such as Shri Krishnaswamy Report, the various reports of State Finance Commission, and also the Report of the Working Group on Local Bodies in Karnataka. Review of this literature would be an integral part of the study.
2. Qualitative data will include interviews with officials and political executive and quantitative data will pertain to the existing data on all the four aspects mentioned in the scope of the study.

3. We will be concentrating on one district in Karnataka where district level planning is done. And choose two taluk Panchayats within it and two villages in each taluk panchayats. We will thereby studying four village panchayats, two taluk panchayats and one district. The criterion to select these will be developed after the initial discussion with state level officials.

4. During the study process we will be exploring with the stakeholders what is the existing practice and what improvements can be done, in district level budgeting and planning with a view to steps, even drastic measures that need to be taken, regarding the same.

5. Policy recommendations of the study will be laid out clearly as they emerge from the study.

**Outcome of the study:** The study will bring out in its report, in comprehensive manner, the nature and problems of district level planning and budgeting. In the process the study will examine the processes of: a) devolution; b) implementation of fiscal measures such as taxation, c) the implementation of central schemes; d) the question of parallel bodies and, e) the question of spatial integration of the plans f) the aspects of dispute resolution; g) the aspect of inter-tier relations h) the aspect of fund-flow from the centre to the states and the i) the question of land acquisition in the case of SEZs and other development projects. This study intends to explore these aspects following the methodology of studying one district in Karnataka; and will study two taluks and four GPs in the process. In doing the above the study will review all the secondary data available at the ISEC pertaining to the district planning process.

We have chosen Tumkur district for study as this district is also the one in which the Institute for Social and Economic Change is conducting the capacity building exercise for Comprehensive District Development Plan (CDDP) and the district represents broadly the socio-economic diversity of the state. According to the district officials
the taluks of the district are classified into developed taluks, backward taluks and most backward taluks. According to this criterion we have taken Gubbi taluk which is moderately developed but a backward taluk, we have taken Kunegal Taluk which is most backward taluk and we have taken Thiptur taluk which is a relatively developed taluk. These taluks also are satisfactory on the criterion of distance from the districts. Gubbi taluk is the nearest taluk to Tumkur district and is 19 kilometers from the district head quarter and consists of 33 Grama Panchayats. Kunegal taluk is 38 kilometers from Tumkur and consists of 36 Grama Panchayats whereas Thiptur is 75 kilometers away from the district headquarter of Tumkur town and consists of 26 Grama Panchayats.

**Tumkur district**

Tumkur is an administrative district in the state of Karnataka. The district headquarters are located at Tumkur. The district occupies an area of 10,598 km² and had a population of 2,584,711, of which 19.62 percent were urban as of 2001. It is a one and a half hour drive from Bangalore, the capital of Karnataka.

The area of the district is 4158 square meters. It consists chiefly of elevated land intersected by river valleys. A range of hills rising to nearly 4,000 feet (1,200 m) crosses it from north to south, forming the watershed between the systems of the Krishna and the Kaveri. The principal streams are the Jayamangala and the Shimsha. The mineral wealth of Tumkur is considerable; iron is obtained in large quantities from the hill-sides; and excellent building-stone is quarried. The annual rainfall averages 39 inches.

There are total 10 taluks in the district. These are 1) Tumkur, 2) Gubbi, 3) Chikkanayakana Halli, 4) Madhugiri, 5) Kunigal, 6) Koratagere, 7) Pavagada, 8) Sira, 9) Tiruvaekere and 10) Thiptur.

From among these ten taluks we have chosen, as already mentioned above, three taluks: Gubbi; Kunegal and Thiptur
Chapter -2

Decentralized Planning in India: Perspectives and Practices

District Planning in India: Historical Perspective

The District Planning as envisaged in the 73rd Constitution Amendment is the outcome various initiatives towards decentralized planning since the process of planned development in post independent India. The need for decentralized planning was first felt during the first five year plan (1951-56), when it was suggested for planning at the national, state, and district and sub district levels. However, the idea was given a concrete shape with the establishment of the district development council to consolidate plans prepared at the village level through a participative process with the establishment of three tier Panchayat Raj Institutions (PRIs) at the village, block and district levels. However, their powers, functions and resources were not clearly defined and as a consequence the planning process at the grassroots level suffered. The Administrative Reforms Commission (1967) stressed on the need for meaningful planning at the district level by focusing on local variations of resources, needs and priorities. Consequently, the Central Planning Commission (CPC) issued guidelines for district planning in 1969, which led to several states formulating district plans. However, the exercise remained on paper in majority of the states due to decline of PRIs during late 1960s and 70s.

The issue of District Planning (DP) has come to surface again, when the working group on district planning headed by C.H. Hanumantha Rao was appointed in 1984. The working group recommended greater decentralisation of functions, powers and resources for meaningful district planning. It also recommended setting up of district planning committee under the district collector. To be assisted by planning officers and technical experts. The other notable committees on decentralized planning are: G.V.K. Rao committee on administrative arrangement for rural development (1985), Dantawala committee on block level planning and the Sarkaria Commission for Centre-State Relations (1988) The second report of economic advisory council under the chairmanship of Chakraborthy has also suggested development planning and implementation with the support of political, technical and financial resources. As a result of these initiatives, the following changes have been observed in the district planning during 1970-80:
1. Identification of district sector schemes.
2. Dis-aggregation plan funds between state sector and district sector.
3. Determination of the share of the individual districts on the basis of selected indicator giving weight to backward areas.
4. Setting-up of district planning bodies.
5. Creation of technical planning machinery at district level.
6. New procedures for the release of funds, their reappropriation etc. (Singh, 1990).

### Box 2.1: Traditional Maharashtra-Gujarat Model (1970s)

Maharashtra-Gujarat Model was good practice in district planning. As per the recommendations of Naik Committee PRI was unveiled in 1962 for local development. Then after 10 years (1972) government realised that district planning is inseparable part of decentralized Planning. After realizing, this government made planning department in state level. So in the same way planning department made district planning boards at district level. The first function District Planning Board is to bring co-ordination with different implementation agencies. Second, giving guidelines to plan formulation and implementation. Third, giving approvals to annual plans and five year plans. We can see that during 1974 DPDC were established in every district. The main function of DPDC was to review on district plan at right time. Overall it was functioning as advisory body. DPDC was formed by district planning Board and District Development Consultative Council. DPDC became watch dog for plan formulation. In this it is said that minister acts as a Palak Mantri and also it includes parliament members, state legislative members, ZP president and CEO, Mayor and Municipal Corporation, Commissioners, members of Municipal Council and officials of co-operative banks.

### Fiscal

Fiscal fund distribution in district planning state government have power to fixed some amount to district planning committees make plan formulation. Here we can observe that there are 3 kinds of schemes viz., national and state sector schemes and district level schemes. From 1970s, onwards discussions on principles and authority of decentralisation became reason for existence of state pool of the district level schemes; in such situation at the district level, state government guidelines are considered to be encroaching on the liberty of the state and frustrates efforts to put substance into planning from below. Here we can notice that there was no importance for block level plan. State government itself prepared to give funds to block level. But yet there are problems. There is no people’s participation related to plan formulation. From this we can observe that there was no importance for PR in Maharashtra. In an empirical study (Gopal, 2000) has identified land mafia found at village and taluk level which highlights weakness of decentralized planning at Taluk and GP level. Also state planning board is not associated with district planning board.

### Gujarat

Gujarat district planning board has broader participatory system. It involves state minister, district planning officer and government staff and also Panchayat presidents and municipality representatives. Earlier Gujarat Panchayat act was not given...
provision to district planning committee but after seeing implementation of DPC in other states. The result of that decision is DPB which makes grass-root level plan formulation and implementation.

District planning board (DPB) formulates plan after organizing on different district level schemes collected from ZP and district level officer. Generally district level officers prepare sectoral schemes whereas Panchayat sectors are prepared by district panchayats i.e., ZP. After organizing these preparations District Planning Board sends it to state level planning for approval.

We can observe that Gujarat district planning board has a problem in allocation. State planning has stopped 80 per cent of allocation related to sectoral planning. This is a problem for development schemes. In remaining 20 per cent DPB allocates 15 per cent to formulation of district level schemes and 5 per cent to formulation on backwardness and it may also consider outlay of state match. By this we can come to know that there are three kinds of outlays and Decentralised Planning is not suitable for integration. And also it has limited authority as it can be expended to non-development; but yet as per DPB guidelines to provide for basic amenities to the people of the district. Because in 1984 some guidelines were formed by reviewing DPB and these made three kinds of schemes: 1, schemes admissible in incentive outlay; 2, schemes admissible in discretionary and incentive outlays 3, inadmissible in discretion of incentive outlay.

**State Plan Out Lay (1985-90) of Actual Plans**
There is a decrease in flow of funds to district level schemes which comes from state plan outlay. In the same way according to a study on district planning there is only 20 per cent of discretionary and incentive fund and also small portion is allocated to local needs and demands. Though tenth finance commission has recommended releasing untied funds, decentralized Planning is getting this fund.

**Karnataka Model**
We can see that among all states Karnataka has taken many steps, efforts to implement decentralized district planning: presence of public representatives along with government officials or bureaucratic and many experiments have been made to allocate funds. The existence of District Development Plan (DDP) was there since 1969 in Karnataka. According to guidelines of planning commission (1969), Karnataka and some other states implemented district plans in a better manner because of this. District and regional planning division existed and also planning departments and district planning officers were found at district level. Deputy Commissioner (collector) was made as leader of district planning committee (district planning officer was seen as member-secretary). This body subsequently was placed before the district developments council. This council had bureaucratic representatives. This system was focused on departmental schemes; though it also involved elected representatives. There was political deficit related to participation in Decentralized Planning. It can be identified in three kinds of stages of Decentralized Planning viz., 1960s, 1980s and 1990s after unification of Karnataka. ZP and Mandal Panchayat were importantly placed with relation to democratic Decentralized Planning. The reason was that ZP had a responsibility of plan formulation and implementation for district development at district level as per the Karnataka Panchayat Raj Act (KPRA). Planning process, in the above scenario of Karnataka can
be categorized into three kinds: state planning at state level, ZP planning at District Level and Mandal Panchayats planning at below district level.

In India the fund allocation was sector-wise an opportunity provided to keep lump sum allocation involving free outlay. But this allocation applied to only state planning schemes and central sector schemes. It was not applicable to schemes of district panchayat level. That’s why it became important later to provide priority to district and panchayat level schemes at district level. And it included ‘Gadgil Formula’ at district level for plan allocation. This has given more preference for backward regions. Because of this 75 per cent of its grants reached to panchayats especially to lower level grass-roots. Along with Gadgil Formula it also included a ‘planning calendar’. We can see two kinds viz., a) monthly multi-level review b) Karnataka developments programme review. Because of this development authority of ZP power has increased and interference of state government decreased. Though in Karnataka there are many developments related to decentralized district planning the outcomes were not all satisfactory.

For multi-level planning system necessary things are co-ordination, formulation and effective implementation and consultation. There should be a planning department at state level which brings effective communication and which has the capacity to handle the difficulties that come at grass-roots level and also it should guide the ZP. According to the Karnataka Panchayati Raj Act (KPRA) of 1993, Zilla Parishad has been changed as Zilla Panchayat and also, in principle, DPC was established to conduct district planning. This gave an opportunity to ZP, TP and GP levels to prepare plans within their limits. This committee involves concerned MP and State Assembly members, ZP, Municipal Corporation and Municipal Council presidents. And also other members (ZP, Nagar Panchayat councilors (Corporation and Municipal) not less than four to five. Along with popular representatives CEO and ZP will be made as secretary and also be included in this committee. They will be named as chief planning officer and other two Deputy Planning Officer and field officers at lower level. These people will prepare plans for district developments. One important point is that there is no importance to TP in plan formulation and implementation. This reveals the fact that there is deficiency in organisation. But yet compared to other states this committee has got more importance. KPRA 1993 established State Finance Commission (SFC) to strengthen District Planning. Though KPRA 1993 has given provision to strengthen Decentralized Planning there are still some demerits: such as a) Involvement of government is more than local representatives; b) ZP and other department official’s authority increased which led to some extent decrease of role and responsibility of president and vice-president of local self governments in Decentralized Planning.

However, all these efforts were not translated into district planning due to decline of PRIs (non-conducting of elections, lack of powers and often resources. The implementation of development programmes outside PRIs was also major cause. The growth of sectoral departments and para-statal bodies (project oriented management for IADP, SFDA, DPAP, DDP, IRDP, watershed and so on), development of sector-
specific schemes and vertical rather than horizontal flow of plan funds were other factors in this regard.

**District Planning Committee**
The 73rd and 74th Amendments in 1992 provided the much needed constitutional legitimacy to Local Governance Institutions to establish District Planning Committee (DPC) to prepare and integrate plans for both rural and urban areas. In spite of this constitutional provision, decentralized planning is yet to become effective in many states. Most states introduced PRIs according to constitutional amendments; state finance commissions for devolution of financial resources were formed (see Table, 2.1 & 2.2 below).

The second round table meeting of state ministers of PR held in Mysore in 2004 recommended for constituting DPCs by 2004-05. The expert group for the grassroots level planning chaired by Ramachandran (2005) laid out the modalities for preparing perspective five-year and annual plans (Box, 2.4). The DPC should be provided with a secretariat. The DPC can take the assistance of technical and academic institutions and experts to perform its functions effectively. The group laid out detailed guidelines for the district level planning process. Another significant measure to push for the activation of DPCs is the linking of access to the backward region grants fund (BRGF) scheme. It is a semi-tied fund available to 250 selected backward districts with the purpose of catalyzing development by providing infrastructure, promoting good governance and agrarian reforms, and capacity building for participatory district planning (Box, 2.5). These plans will put together resources from various existing schemes and channels them to panchayats on the basis of the district plan. BRGF funds will be used by the panchayats for gap filling and to converge and add value to other programmes, which provide much larger resources to the same districts. States were also required to outline their functions, procedures and agencies for district planning. The states were requested to provide untied funds to Local Government Institutions.

**District Planning Committee: Inclusiveness, Autonomy and Accountability**
The preparation, implementation and outcomes of the district plans depend on the autonomy (powers and resources), inclusiveness, capacity and accountability of the DPCs. The issues raised are: Whether the DPCs are constituted? Whether they are
functioning? Whether they are democratic, inclusive? Whether they are autonomous? Whether they are professional? Whether they are representing the aspirations of the people?

**How Democratic and Inclusive DPC?**

Majority of the states, {11 out of 18 states} DPCs have been constituted, although there is variation across the states in regard to powers, functions and composition (table 2.1 and Box, 2.5).

DPCs are constituted through the elections to make it more democratic and inclusive. At least four-fifths of the DPC members are elected from Local Government Institutions and the remaining members are to be nominated. States like Karnataka and Himachal Pradesh (HP) follow this criterion and restrict the nominated members to 20 per cent or less. While all DPC members are nominated in Jharkhand. The nominated members are usually from the government non-government and academic and research institutions. The special and permanent invitees generally include local MPs and MLAs, district officials, representatives from District Cooperative/ Land Development Banks without voting rights. Election to the DPC is not uniform across the states. In Kerala, in fact, DPC elections are synchronized with local government elections. While in states like Karnataka, CEO acts as an electoral officer for conducting elections. Elections are held on paper. In fact many members are not aware of the elections. In some cases, elections are unanimous. For instance, the election held in Mysore in 2004 was unanimous. In some states district minister is made the Chairperson of the DPC.

Reservation is provided for disadvantaged (women/SC/ST/OBC) to make more inclusive in some states. For instance, 50 per cent of seats are reserved for women in Bihar as against 20 per cent in HP and 3 seats in Chhattisgarh. No such reservation exists in Haryana, Rajasthan and Kerala for women.

**Box 2.5: District Planning Committee**

The constitution of DPCs recognizes the need for integrated regional planning based on the investment patterns, its spatial impact and development. The DPCs should be
vested with enough powers to undertake the following functions, besides preparation of draft development plan for the district.

Preparation of draft development plans including and integrated spatial plan for the district, keeping in view matters of common interest between Panchayats and municipalities.

The DPC should provide advice and assistance to local bodies in preparation of development plans and its effective implementation.

The tasks of DPC include coordination and monitoring of the implementation of District Development plans.

Allocation of resources to local bodies for planning and implementation of local level projects contained in the District Development plans.

In Punjab, DPC consists of 15 members representing district population of not exceeding ten lakhs; 24 members for ten to twenty lakhs; and 40 members exceeding twenty lakhs. The Chairperson of the DPC is nominated by the state government from its members. The members of the DPC are elected and nominated. Not less than four-fifths of the DPC members are elected by and from amongst the elected members of the panchayats and municipalities in proportion to the ratio of rural and urban population. One-fifth of the DPC are Members of the Legislative Assembly and other persons are nominated by the Government. The Deputy Commissioner is ex-officio Secretary of the DPC. The Additional Deputy Commissioner (Development) is its Additional Secretary. The Deputy Economic & Statistical Adviser is its Joint Secretary. The term of an elected member is co-terminus with their term. The term of a nominated member including the Chairperson is one year. However, a nominated member shall be eligible for re-nomination after the expiry of the tenure of the committee.

**Functions of the DPC in Punjab:**

a) to prepare the draft development plan keeping in view the matters of common interest between urban and rural population including integrated spatial planning regarding matters such as sharing of water and other physical and natural resources, the integrated development of infrastructure and environment conservation, the plans prepared at the grass-root level by the Panchayat and the extent and type of available resources whether financial or otherwise;
b) To prepare priority-wise list of schemes and programmes taking into account the resources available with the DPC and the resources provided by the State Government.

c) To take appropriate measures for proper implementation of the development schemes, programmes and projects;

d) To monitor the progress of projects;

e) To encourage the Panchayats and the Municipalities to take up and expedite the implementation of development projects;

f) To make efforts to generate additional resources for development works with the cooperation of people; Non-Government Organizations and Non-Resident Indians and other agencies; and

g) To perform such other additional functions relating to district planning and coordination and monitoring of the activities of different departments of the State Government;

(2) While preparing the draft development plan, the DPC may consult such institutions and organisations, as may be specified by the State Government from time to time.

(3) The Chairperson shall forward the district development plans prepared by the DPC to the State Government.

How Competent and Professional DPC?

The competency of the DPC depends upon the supporting professional/ technical staff or technical advice received from the outside. Different arrangements have been made for DPCs to obtain technical support for performing their functions. To prepare the plan, they need to independently conduct studies, as at present the DPC is not equipped with experts and required personnel. Under the guidelines, expert committees for each core area such as poverty alleviation, health and sanitation, education etc., need to be constituted. The members of these committees will be drawn from the departmental officers, NGOs, elected members of the DPC. In Karnataka so far these committees are not constituted in some districts such as Mandya. Where as these committees are formed in Mysore district DPC, but not yet functional.
In Kerala, as discussed earlier, the DPC is assisted in scrutinizing plans and projects by Technical Advisory Committees (TACs). The TACs have sectoral sub-committees to study the respective chapters of the district plan – for example the municipal TAC for urban plans, under the guidance of district level TAC. The DPC also consults with their working groups of technical experts as and when necessary.

In Rajasthan, different means have been adopted by DPCs for technical support. Plan consolidation work is being carried out by the chief planning officer of the district. The DPC can also hire experts as consultants. Heads of all line departments are often invited in DPC meetings (as reported from Karauli district). In Karnataka, DPCs can constitute expert committees, and can also hire technical experts if they feel the need. In Karnataka a major limiting factor has been the lack of planning skills among the members. The members have voiced the need for support staff and regular financial inflow for the DPC, the absence of which is an inhibiting factor in the performance of the mandated functions by the committees.

In most of the states, DPC at the district and sub district level is supported by planning staff and a majority of them are drawn from the statistical department as is the case also with Karnataka. In some states, he is designated as member-secretary to the DPC, whose function is to maintain the records of the committee and taking care of other ancillary matters. In some states the DPCs are also provided with secretariat or support departments to help in their functioning, either through new secretariat, or transfer of existing administrative departments to their jurisdiction. Similarly, taluk planning officer positions are filled in 93 backward taluks out of the state in Karnataka. The availability of funds with them enables them to do so with ease. Issues such as the need for technical support to DPCs and their capacity building will be more significant and effective but only, when the DPCs become functional.

**How autonomous and accountable DPC?**
The autonomy of DPCs is assessed in terms of powers and resources enjoyed by the DPC in formulating district plans. The accountability is assessed in terms of the extent of fulfillment of the tasks entrusted to it and a mechanism through which the DPC is answerable. In majority of the states, DPCs have been entrusted with adequate
powers and resources. The chairperson of the DPC and the manner in which she/he is appointed is also an indicator of the degree to which the DPC is actually an independent body. In some states (Kerala, Bihar, Karnataka, Andhra Pradesh, Rajasthan, Tamil Nadu and West Bengal) the chairperson/ president of Zillah Parishad (ZP) is the chairperson of the DPC. In states like Orissa, Gujarat, Madhya Pradesh, Chhattisgarh and Maharashtra, minister-in-charge of the district or any other state minister is the chairperson of the DPC (Decision making within the DPC is dominated by the minister. All plans are made with her/his approval and suggestions by other members are generally not taken into account).

While in Haryana, the Deputy Commissioner (DC) of the district is the chairperson of the DPC. Secondly, the DPC has no resources at its disposal. In Kerala, the chairperson is president of the ZP and vice chair person is an expert, unlike the situation where often the latter is president of the municipal corporation.

The system of having state ministers as chairpersons of DPCs severely hampers the participative nature of the planning process in the DPC. DPC members reported that decisions were unilaterally taken by the minister-in-charge of the district (who is the chairperson) without heeding suggestions from other members. Hence the decisions often did not reflect the popular opinion.

Apart from the above funds, the state government may at its discretion provide financial assistance for effective functioning of the DPCs. But, so far the DPCs have not got any additional funds from the state or central government. When a question was posed to the members on why they need funds, many of them expressed that funds are necessary to prepare and implement the plan.

The main concerns expressed by stakeholders regarding the powers and resources are as follow: Firstly, DPC members feel that they do not have any say in deciding beneficiaries of various schemes, which often do not reach the right people. Secondly, people are not serious about district plan due to lack of financial resources and powers (financial contributions from all local bodies are irregular to support the planning process). Thirdly, Panchayat level plans are not being effectively integrated with state plan because of ineffective DPCs and imbalanced plan priorities.

Several concrete steps need to be taken to further strengthen and decentralize the institution of DPCs. In order to give them a truly representative and participatory character, it is extremely necessary that practices such as appointing state ministers as chairpersons, or nominating all members of DPC, need to be put an end to. The
government might consider introducing some disincentives for states adhering to such practices. Certain constructive measures that need to be taken in order to strengthen DPCs include the following:

The DPCs need to be given adequate financial support as well as staff strength in order to enable them to perform their tasks effectively. Converting DPCs into permanent institutions with offices and secretariat will perhaps address this issue to a large extent.

**What role DPC has been entrusted?**

The clarity about role and responsibilities of DPCs has a bearing on its performance. DPCs prepare draft development plan by taking common interest of PRIs and municipalities for effective utilization of physical and natural resources for infrastructure development and environmental conservation.

In Karnataka, DPC prepares 20 years vision plan, 5 years development plans and annual plans. It also reviews implementation of development plan periodically and monitor achievements. In Kerala, the DPC monitors the quantitative and qualitative progress in the implementation of plans.

The only function that the DPCs have performed is approval of annual budgets of the rural and urban local bodies.

**Does DPC have the capacity?**

Institutional capacity building has to be coterminous with capacity building of members and expert associates. Clarity of roles and responsibilities is required to bring vitality to the DPC as an institution, wherever functioning. The need for official and non official members to understand the role of the DPC, the nuances of integrated planning for social change and the difference between perspective, five year and annual plans is essential.

In Kerala’s initial ‘campaigning’ mode to shakeup the system, it was observed that ‘panchayats could not cope with the administrative or organizational challenges of spending the money (nearly one to one-and-a-half crore Rupees per panchayat per annum) allocated to them’ through the people’s plans. The campaign had risen people’s expectations to a level much beyond what the local bodies were equipped to deliver. The campaign approach is, however, useful for generating awareness among the people’s and ensuring participation in the district planning process, and therefore, should be adopted in other states as well. However, it can be taken up after the
institutions are equipped to respond to people’s plans as well. The rural and urban local bodies also need to be oriented to adopt an integrated approach to planning.

While preparation of annual plans they have to keep in mind the medium and long term vision and goals for the district. The planning function in urban areas itself suffers from ambiguity in the sense that land use planning is often centralised under the town planning department, and the ULB only carries out annual budgetary planning. In some cases para-statal bodies carry out independent planning for the services they provide, especially such as water supply. In such a scenario it is very important to ensure that all such multiple bodies carry out the planning exercise together, keeping the district long and medium term perspective plan in purview.

How Effective are the DPC Deliberations?
On the whole the DPC has not been very active in many states. According to many studies, DPCs are existing only on paper and do not function on the ground. This is the situation in states, where DPCs are constituted. For instance, the DPCs in Karnataka were constituted quite early as compared to other states, that is, in 2002. However, since then the DPC in Mandya has met only thrice while the Mysore DPC has met four times. The five-year plans for the districts have not been prepared by them.

All members do not participate in DPC meetings. Members are often not aware of the annual plans for their districts. Awareness among local government officials regarding existence of DPC is low. The average attendance in the meetings is 16 out of 25 members, which is slightly more than 50 per cent. Departmental heads from all concerned line departments were also attendees and discussants in the meetings. Besides, often decisions are taken unilaterally and then circulated among members for signature. DPC meetings have been mostly focused around seconding proposals for utilization of untied funds available under the district plan. The planning process in the DPCs is heavily focused on schemes and works (PRIA, 2009).

How Plans are Prepared?

<table>
<thead>
<tr>
<th>District Development/Perspective Plan (15-20 Years)</th>
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<tr>
<td>Short Term Plan/Action Plans/Annual Plans</td>
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The preparation of short term plans involves the process of identification of problems, setting objectives, developing options, prioritization, choosing/deciding the option, plan action, implementation, operation and maintenance. The monitoring and evaluation is a continuous process from the beginning to end. The municipalities and the Grama Sabhas have to prepare the short term action plans. Since the ward Sabhas have not been set up in urban areas, the municipalities have to prepare the action plans. The steps in the preparation of action plans/short term plans are illustrated in the figure below:

**Steps in Action Plan/Short Term Plan Preparation:**
Implement prioritize and choose plan action develop options operate and maintain medium identify problems setting objectives monitoring and evaluation medium term plan short term plan.

**Medium Terms Plans (3-5 Years)**
A medium term plan of 3-5 years focuses on achieving prioritized objectives. It normally comprises a number of programmes and projects which are closely tied into the commitments – institutional and investment including government which is necessary for implementation. A medium term plan may consist of more than one action plans. A medium term plan could comprise a number of multi-sector investment plans that are drawn from different sectors such as infrastructure, poverty, housing, health etc.

District planning can be successful only when it is owned by all the stakeholders – both people and planners alike. Hence, all round awareness and education is a necessary precondition to make it effective. In this context the last point could be that if all recommendations of the expert group on grassroots planning are implemented with sincerity, then perhaps by the end of the eleventh plan period, DPCs will surely emerge as central institutions of grassroots planning in India\(^1\).

**District Development Plan**
District development plan should be a statutory development plan for a period of 20 years. The district development plan should be evolved based on the action plans and medium term plans of the rural and urban areas. The medium term/multi-sector plans requiring investments of different magnitude and based on their priority are spread

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across a scale of 20 years. This perspective/development plan is prepared based on the action and medium term plans prepared by the local bodies and various departments. The implementation of this plan should be supported with statutory/legal support. An independent authority within DPC comprising professional planners, engineers, and financial experts etc., headed by the DPC chairperson should be set-up to monitor the implementation of plan. The successful implementation of the plan is dependent on full co-operation of the various stakeholders, proper integration of the plans, the commitment of the members of the DPC and the sub-committees involved in the planning, convergence of resources from the multiple organizations in rural and urban areas including the government schemes to achieve common objectives and good coordination.

The guidelines for decentralised planning process under the Eleventh Plan period are available. According to the guidelines, the Local Government Institutions (LGIs) formulate vision documents as well as five year development plans and annual plans. The district annual plans will be based on the guidelines and annual plan ceilings fixed by the state governments. For instance, in MP the DPC finalises sectoral plan allocations for rural and urban areas with the line departments. The DPC also assesses available resources in the district with the help of an expert group. Each local body prepares plan with in the plan ceiling set by the government. DPC will help integrate the rural and urban plans assisted by a planning support group which can include subject experts and local Civil Society Organizations as well. This integrated district annual plan will then be submitted by the DPC to the state planning board.

As per field information, this process does take place in the districts. DPCs meet and approve district plans, which are then further submitted to the state planning board. However, the plans themselves are weak and lack integrated approach. Planning has become more of a procedural formality rather than meaningful planning. There is a strong requirement of all-round orientation of all stakeholders in the district planning process in the state, to make it meaningful and realistic.

The plans in Rajasthan are prepared sector-wise and area-wise by the DPCs as per the ceiling on budgeted amount fixed by the state. Proposals are invited from heads of various departments and the funds are then disbursed accordingly. 17 sectors have
been identified for preparation of district plan. The plans prepared were stipulated to follow the participatory process, and needed approvals from the local elected bodies. The process did take place, but there is no accounting for its participatory nature. Panchayat and ULB plans were integrated into block level plans and then forwarded to chief planning officers who consolidated them into the district plans. These were then approved formally by the DPCs.

In Karnataka it is the sole responsibility of the DPC to prepare the district plan. The development plan has to be based on the perspective plan prepared by it. A separate urban unit has to be formed for preparation of urban plans. DPCs can seek the support of experts and technical agencies for plan preparation. Expert committees can be set up for each core area such as health, education, water supply, poverty alleviation etc. The members of these committees can be drawn from line departments, NGOs, private agencies, district administration and elected members. The DPC also needs to periodically evaluate progress of the plans and projects in the district. To carry out their functions effectively, the DPCs have been given financial power by providing them with a DPC fund. This fund consists of annual contributions of fixed amounts from various local bodies in the district.

The setup for DPCs is thus elaborate in Karnataka. For example the Mysore DPC constituted several committees – on agriculture, poverty alleviation, health, education, social justice, infrastructure services and administration. These committees are working towards preparation of 20 year perspective plan for their respective sectors. No such effort has taken place in Mandya. Effective convergence of rural and urban bodies as well as line departments for integrated planning is also not visible.

Kerala’s approach to initiating the process of grassroots planning was in the form of a year long People’s Campaign for Planning launched by the Kerala planning board. The campaign mode helped to build mass awareness and participation in the decentralized planning process when it was initiated for the first time in 1996. Development seminars were held as mass public events for multi-stakeholder consultations. Volunteer technical corps comprising both serving and retired officials helped ensure that the people’s plans were technically and financially viable. These were then finally cleared by the DPCs. This mass campaign mode helped mobilise people towards a common cause of planning from the grassroots. As per the current planning procedure in Kerala, at the intermediate level there is a Technical Advisory
Committee (TAC) to vet and verify the plans prepared by GPs and recommend to the DPC for approval. All the plans of GP, block Panchayat, urban local bodies and ZP reach the DPC and the TAC then verifies the plans. Integration is made at the instance of the TAC and the Plan Preparation Support Group (PPSG). The DPC consolidates the plans received from local bodies within the district and submits the same to the state government.

### Planning Processes at the Grassroots

As per planning Commission guidelines, district planning is the process of preparing an integrated plan for the Local Government taking into account the resources available and covering the sectoral activities and schemes assigned to the district level below and those implemented through local Governments in the state.

The document that embodies this statement of resources and their allocation for various purposes is known as district Plan. The following three aspects are essentially required for preparation of district Plan:

- Plan to be prepared by the Rural Local Bodies for activities assigned to them and National / State Schemes implemented by them with their own resources and those earmarked for these purposes.

- Plan to be prepared by the Urban Local Bodies for the activities assigned to them and National / State Schemes implemented by them with their own resources and those earmarked for these purposes.

- Physical integration of plans of rural and urban Local Bodies with the elements of the State Plan that are physically implemented within the geographical confines of the district.

All these three aspects are to be considered and consolidated by the DPC into a district Plan. Decentralized planning is to be arrived at by an integrated participatory and coordinated idea of development of local areas. Each Gram Panchayat or Municipality is treated as a planning unit and district plans are prepared through consolidation and integration of these plans as well as by considering the development of district as a whole.

To ensure the use of resources available at the local level and resources made available under various schemes in a better way, that the development needs as desired of the whole district may be achieved. Decentralized planning ensures better
delivery of services and efficient use of resources whether financial or otherwise. It leads to higher growth rate in the state. Qualitative improvement will also take place as the felt needs of people as reflected in the plans will get fulfilled.

In Kerala the process of planning is as follows. Sectoral sub-groups and working group prepare draft plan which is then approved in gram sabha meeting. sectoral discussions in villages/ ULBs on 17 identified sectors – demands not being met by all sectors were also recorded rural-urban linkage consolidation only at DPC level by PPSG defined by community needs/ ensured by Block and DPC panchayat level plan joint meeting of panchayat committee and working group draws up final panchayat plan – this is then again vetted in a development seminar with all stakeholders on board at panchayat samithi level sectorally approval to panchayat/ block plan vetted by block level TAC and block level gram sabha by block officials – through vetting and consolidation of panchayat and city plans, the district plan is finalised. All rural plans integrated to district panchayat plan; municipal plans undergo same process prepared by chief planning officer of district by consolidating block plans final submission DPC approves plan in consultation with district level TAG and submits to state planning board DPC approves integrated plan and submits to state government institutional arrangement. PPSG (to finalise sector-specific district plans) coordination committee–state, district and block level technical support technical support group, TAG, TAC expert services; participation by departmental officials V.3. Role of DPCs with respect to rural and urban local bodies DPCs play an anchoring role between panchayats and ULBs. They help provide the common platform for integrating rural and urban plans. They help identify planning projects of common interest and spread across both rural and urban areas, which can be jointly planned and funded. This could include extending link roads from rural hinterland to urban markets, or extending water supply and sewerage infrastructure to peri-urban areas.

**District Plan Procedure adopted** 17 sectors have been selected for preparation of district Plan. These sectors are agriculture, animal husbandry, energy, ground water and drinking water, education (higher, technical and elementary), medical and health, rural development, sanitation, industries, roads and bridges, nutrition, urban
development, forest, cooperative, PDS, water resources and others like banking sector.

The guidelines and formats were circulated to the districts for district Plan.

- The training programme organized at State, district and Block level.
- The concerning officers and personnel were trained to prepare the district Plan and fill up the prescribed formats.
- A time bound programme was prepared and circulated to all concerned.
- Wide publicity in Gram/Ward Sabhas was done so that wider participation of the villagers and urban people as well as functionaries and public representatives could be possible.
- Gram/Ward Sabhas organized as per scheduled programme.
- Village/ULB level functionaries of the selected key sectors in the Gram/Ward Sabha held the sectoral discussions.
- During the discussions the plan objectives and prioritization were explained by the Government functionaries and got approval of community. The community has determined the village/urban needs prioritization and linkages.
- The village/ULB plans approved by Gram/Ward Sabha are integrated into panchayat/ULB plan at the Gram Panchayat/ULB Level and prepared the panchayat/ULB plans.
- The services of experts have been allowed to prepare the Plans.
- The Panchayat Samithi level infrastructure demands were got assessed and approved in the General Bodies meeting of the Panchayat Samithi. Similarly the Urban Local Body level
- Infrastructure demands were got assessed by the Urban Local Bodies and approved by the Boards of the concerning local bodies.
- The Block level sectoral officers on the basis of their departmental norms did the prioritization and technical vetting of the Panchayat Plans.
- A separate list of the requirements which were identified at the panchayat level but not fulfilling the departmental norms but were otherwise justified was prepared along-with requirement of funds for these demands.
The block level draft plans prepared by integrating the Panchayat and ULB plans and Panchayat Samithi level demands were provided to Chief planning Officers.

By integrating the block level plans, the district level plans have been prepared by Chief planning officers and have been approved by DPCs.

Both the urban and rural district Plans have been integrated at district level.

**How effective is the integration of urban and rural planning?**

We must understand the fact that the planning is not for planners, and planning is not just spatial planning or land use planning. It is sum total of physical, spatial, economic, financial, social and institutional planning. In the existing institutional set up, the integration of these planning components has become difficult for the DPC. The rural and urban local bodies including the government departments have resorted to routine annual budgetary plans which they find it easy. And these annual budgetary plans are placed before the DPC for customary approval.

DPCs have not been able to effectively enable rural-urban linkages. Coordinated planning is not taking place, and any joint project planning has not necessarily resulted in integrated project implementation. Several reasons account for this. Rural and urban local bodies are not working together on a common platform during the planning process to identify common projects/ resource requirements. The plans made in isolation cannot be implemented in an integrated manner. Urban local bodies have traditionally been oriented towards the state directorate/ departments of urban development – hence plans are submitted at the state level apex body for ULBs rather than DPCs – the vertical line of accountability still persists in spite of the revised planning process. This problem has been observed in district planning in Karnataka. Block-level integration of rural and urban plans is not carried out – the DPC guidelines recommend direct transmission of ULB plans to DPC. This may be a hindrance to effective integration of plans at the block level, which may be important especially in the case of small towns. These small towns have significant linkages with surrounding rural areas since they serve the purpose of market centres for the rural hinterland. Inter-sector coordination was also felt to be a problem since it was
resisted on account of being against the status quo – old procedures are being followed for the sake of convenience as well. For example, the planning process of schemes like NREGA, SSA, NRHM and JNNURUM, wherever undertaken, is often independent of annual planning at Panchayat or municipal levels.

Has this integrating function been effectively performed in the DPCs studied? The answer is not definitive. In Mysore and Mandya DPCs, no evidence was available on consolidation of rural and urban plans, or any joint planning. The Mysore DPC in fact noted with concern that municipal plans were being placed before the State Directorate of Municipal Administration rather than the DPCs. Mutual coordination and sharing of plans/projects was not visible in both districts. Even if planned with rural-urban coordination, projects had to be implemented separately by rural and urban local bodies, and hence the goal of integrated development was not being met. In Rajasthan, information available on the meetings held in DPCs of Jhunjhunu, Tonk and Karauli this year does not relate to the process of integrated rural and urban planning. Hence, the anchoring role of DPC is not reflected in the data available. The annual plan of 2006-07 was approved in one meeting of Jhunjhunu DPC, which showed detailed sector-wise allocations. In Kerala, the DPC is acting as a plan scrutinising body at the district level – to what extent does it play a meaningful anchoring and integrating role is not clear.

**Link with sectoral plans:** The planning process being carried out in the district is largely sectoral and the DPCs play an instrumental role in integrating sectoral plans for a unified district plan. Different states have provided different instruments to do so. In Rajasthan, it was observed in all three DPCs that officials from all the line departments were invited to the DPC meetings and hence participated jointly in the discussions on district plan. In this way DPC could monitor implementation of sectoral plans and schemes. In Karnataka, the DPCs can form sub committees with officials and experts for different sectors to facilitate plan preparation, monitoring and implementation. Mysore has formed seven such committees but none are functioning. Mandya is yet to form any. This implies ineffective role being played by DPCs in integrating sectoral planning at the district level. The Karnataka study notes that even experts engaged by the DPC for sectoral planning were not necessarily adept in integrating the sectoral plans, and hence needed additional capacity building for comprehensive social, economic and spatial planning.
Kerala has the system of Technical Advisory Committee with sectoral sub-committees to study sectoral aspects of the plans. Integration of plans takes place only at the district level. As per latest state government guidelines, sectoral research teams can be formed under the plan preparation support group to aid the process of preparation of annual plans by all local bodies in the district. All these various means for enabling DPCs to integrate sectoral planning have been devised by the states, but their effectiveness depends on how effectively the DPCs are able prepare district plans. This remains to be seen.

Observations based on studies conducted by PRIA:

- Functioning of DPCs is not satisfactory. The planning at present takes place in a disjointed approach in the urban and rural areas. For instance, the projects of water supply, roads, schools, or hospitals etc., are implemented by the respective municipalities or the Grama Sabhas.

- At present, not much co-ordination is visible. There is a need for co-ordination of mutual sharing of amenities. This could be done by the DPC at the time of preparation and implementation of new plans. The individual municipalities or the rural local bodies could request the DPC to co-ordinate the common issues that could effectively solve conflicts and enable them to share resources with mediation of DPC.

- The DPC is constituted with elected members and all of them need basic training. There is a need for orientation on planning and why and how the short term, medium term and long term plans are prepared and implemented?

- The objectives and role of the DPC and its members need to be made clear.

- The local bodies have to evolve strict measures to collect internal resources. The resources generated internally and externally should be enough to meet the local plan implementation. But at present, internal resources collected by them are not sufficient. External resources are not adequate and dependent on the state and central government or external agencies.

- The expert committee members drawn from the departments and NGOs including the elected members need basic training in the integrated action planning, medium term planning and long term planning.
Training in planning for social, financial, spatial, physical, economic requirements etc., need to be given to all the experts and elected members of DPC.

In all the meetings that are conducted, the focus is only on the rural development and projects related to rural areas. Focus should be on the entire district development, which includes both urban and rural development.

So far the feedback is that DPC is concentrating more on the matters of individual projects and schemes of rural development. Focus should be to prepare the medium and long term plans within which the annual plans are to be chalked out for both rural and urban areas.

The expert sub committees have been formed in Mysore. But they are yet to prepare the plans. These sub committees are to be legalized and adequate legislative binding need to be placed over them in order to make them prepare and implement plans.

The DPC needs to be strengthened with adequate technical and managerial and financial support from the town planning, engineering, financial, economic and social and all other departments of the government.

It is seen from the discussion that the ULBs and the rural local bodies are preparing their own annual plans without considering the medium and long term vision and overall integrated development, which are just placed before the DPC for customary approval. This needs to be reviewed in the context of the DPC’s role.

Each sub committee should have experts such as planner, financial expert, economist, engineer, developmental expert, socialists, NGO representative, representatives from private firms and all the related departmental experts.

The training should be tailor-made in two phases, first phase training is on the planning process and preparatory work for the different plans, and the second phase training could be after a gap of three months on preparation of plans based on the data and preparatory work the members have carried out.

Once the plan is prepared by the DPC, implementation plan is to be prepared. The long term plan is sum total of medium plans and short term action plans.

The focus should be on implementation and monitoring, and monitoring has to be constantly done to review and modify the implementation process to get the desired output.
At present the representation of urban local bodies in DPC is negligible. There are only three to five members. It is essential to give equal thrust to urban areas as they could act as engines of rural development.

The PURA (Provision of Urban Amenities in Rural Areas) concept and scheme needs to be fully integrated into the medium and long term plan of the district.

All the central and state government schemes and projects meant for the rural and urban areas have to be scanned and brought under one roof so that these schemes are implemented in an integrated manner to achieve the long term objective of the planning development plan.

The planning Officers are to be made responsible to implement the plan as per the time schedule of the plan implementation.

**B. Metropolitan Area Planning Committee**

The constitution of MPCs in every metropolitan area under Article 243 ZE of the 74th Amendment accords constitutional recognition to metro-regional planning when seen in the context of agglomeration economies, a metro region is the most preferred area for investment in economic activities and infrastructure but these areas are normally deficient in spatial planning inputs. The functions to be assigned to MPC are as follows:

1. Preparation of draft development plan for the metropolitan areas.
2. Spatial coordination of plans prepared by the municipalities and panchayats in the metro area and recommending modifications in local area plan, if any taking an overall view.
3. Advice and assistance to local bodies in preparation of development plans.
4. Monitoring effective implementation of approved development plan of the region.
5. Undertaking formulation and implementation of projects involving provision of infrastructure such as major roads, trunk services, electricity, telecommunications, etc.

The 12th Schedule of the Constitution (74th Amendment) Act lists the 18 functions of the municipalities which among others include: (I) urban planning including town
planning; (ii) regulation of land use and construction of buildings; and (iii) planning for economic and social development. In this regard, the state governments could be more specific and definite in assigning functions to the local bodies. In the absence of clarity in assignment of functions, the State Finance Commission would not be able to assess the fiscal needs of and allocate adequate resources to the municipalities. For a rational integration of spatial and economic development, functions related to spatial and socioeconomic planning and development should be assigned to Urban Local Bodies (ULBs). To facilitate the municipalities to discharge these functions, a provision could be made in the State Municipal Acts for devolution of necessary power and authority along with financial resources and manpower. For an effective urban planning system, there is the need to have a package of inter-related plans at three levels namely long-term perspective structure plan (20-25 years) short term integrated infrastructure Development plan (5 year) and Annual Action plan as part of Infrastructure Development plan. The short-term integrated Infrastructure plan and Annual plan could be in the form of “rolling” plans to enable the ULBs to continuously review and monitor the plan, and to update it every year / five years. The aim should be to make urban planning system as a continuous process. Each level of plan must include measures for infrastructure development and environmental conservation:

**Perspective Plan.** The long-term Perspective Structure Plan could be prepared by the MPCs broadly indicating goals, policies and strategies for spatio-economic development of the urban settlement. The perspective plan may include:

1. Physical characteristics and natural resources:
2. Direction and magnitude of growth and development – area and population (Demography)
3. Arterial / grid road network and mass transit corridors with modular development block.
4. Infrastructure network – water, sewage, drainage, roads, bus and truck terminals, rail network, etc.
5. Broad compatible and mixed land use packages and zones :
6. Community open space system and organization of public spaces :
7. Environmental conservation and preservation of areas of architectural, heritage and ecological importance ;
8. Major issues and development constraints;
9. Financial estimates and fund flow patterns; and
10. Policy and plans for EWS housing.

2. **Infrastructure Development Plan**: Integrated infrastructure Development Plan should be prepared by ULBs in the context of the approved Perspective Plan. The scope of the Plan should cover an assessment of existing situation, prospects and priorities and development including employment generation programs, economic base, transportation and land use, housing and land development, and environmental improvement and conservation programs. The development plan may include:

- Identification of gaps and shortcomings in the delivery of municipal services;
- Identification of service and remunerative projects and their prioritisation along with capital budgeting and investment programmes; and
- Housing and land development programmes, including identification of areas for residential and non-residential development and development of trunk infrastructure.

1. **Action Plan**: Within the framework of Development Plan, Annual Action plans for the urban areas should be prepared by the ULBs specifying the projects and schemes with costing and cash flow for both on-going and new projects. The Annual action plan should provide an in-built system for implementation of the Development Plan. In this plan various urban development schemes should be integrated spatially and financially. Annual plan may consist of:

- targets to be achieved – physical and fiscal;
- fund flow; and
- project design and specification, including tender document for implementation.

3. **Projects and Schemes**: As part of the Development plans and Action plans, projects and schemes within towns / cities could be taken up for any area / activity related to housing, commercial centers, industrial areas, social and cultural infrastructure, transport, environment, urban renewal etc. by governmental bodies / local agencies / private sector and through inter-governmental public private-
partnership. Such projects could be both long-term and short-term and in conformity with the development requirements of the respective town / city.

Scholarly Literature
In the following review of scholarly literature and here we have two broad sections. One that deals with the generic problems with district level planning and budgeting in the country; and the rest are case studies done by specific scholars on specific states. The second section deals broadly with the scholarly studies of Karnataka, Kerala, Uttar Pradesh, Madhya Pradesh and briefly, West Bengal. In the following we begin with the generic problems that are identified by scholars followed by specific case studies. Since the literature related to local self-government is vast we had to limit ourselves to important and pioneering states in district level planning.

District Planning and Budgeting Process Some Generic Problems
Vinod Vyasulu (2007) has suggested how decentralisation and its financial aspect could be strengthened; the main recommendations that Vyasulu makes are as follow:

1. PRIs work nature must meet in a democratic ways: regular meetings and its minutes, later with changes and approved minutes should be passed; there must be coordination between elected bodies and officials in respect to decisions and to encourage people’s participation.

2. The examples of states like Madhya Pradesh and Karnataka are to be followed. Panchayats conduct survey of their constituencies for plan regarding health, education and biodiversity. Karnataka is also one of the best examples for watershed and forests but in this case there is a lack of coordination between line departments and Panchayats. Whereas in the case of MP government is not involved and Panchayats do not have any clashes.

3. There needs be budget session on finance at all level of PRIs. This will help local levels to get knowledge about sources: where the resources come from, what are the conditions; and how to use and how to distribute and expenses on priority basis etc.

4. In funding pattern there should be feed back.
5. To improve horizontal integration there should be discussion on expenditure. This encourages elected bodies to take responsibility also leads people to get involved in development matters.

6. Encouragement should be given to revenue collection at third level tier.

7. The district statistical departments need to have well equipped advance computerization for all data sources for developmental purposes.

8. To introduce inter-district council body can build a good network in plan formulation and implementation.

Another study by Vyasulu (2003) found that local bodies are very weak in collecting taxes; also flow of funds from higher levels are often tied to specific schemes. These made financial devolution very weak. The untied funds which they are getting are also not sufficient with irregular timings to fulfill their needs of development. Here we can find that the lower level is denied its freedom to fulfill its functions and duties.

Devendra Babu (2008) has found certain generic problems and prospects of district level planning and these problems and difficulties need to be addressed regarding the autonomy of local bodies:

1. First, the state interference through MLAs and MLCs in the PRIs powers, functions and resources is increasing day by day.

2. In the administrative decentralisation PRIs should have their own personnel than being deputed from various government departments’ personnel. So they could have powers to dismiss if they find misconduct.

3. There are many programmes and schemes from central plan schemes, centrally sponsored schemes and state government schemes which are implemented through PRIs; this is taking place without taking into consideration the local level needs. This makes PRIs to act as central or state government agencies. Owing to this there is lack of local level interest. Also there are state government guidelines on expenditure; and nothing remains for after following these guidelines for local bodies to take up new projects at that local level.

4. Parallel bodies are also involved in rural development this could be a danger for grassroots level bodies for their effective role.

5. In grant distribution there is a regional and inter-tier inequality.
6. Often there is lack of numerical as well legislative strength in GS and there is no enforceable power for its decisions.

7. Also District level Planning depends on the effective participation by the elected representatives in planning formulation but most of plans are sectoral rather than integrated, spatial and prepared at ZP level; there is also skill-deficit and there should be skilled planning.

8. There should be collective resource distribution rather than individual distribution of resources.

9. Lack of knowledge on local level functionaries at the local level civil society is a major factor affecting the accountability of local level functionaries.

**PRIIs and local bodies functioning and planning: specific case studies**

**The Case of Karnataka:**
Karnataka has been on the forefront of discussion on the local bodies; particularly so with the rural local bodies. The state has seen many an experiment on decentralisation. In the following we refer to some studies by prominent scholars on Karnataka. Shuba and Bhargava focused on the rural sector. They say that according to the Balwant Rai Mehta committee the main reason for failure of development through PRIIs was because of lack of people’s participation. This Balwant Rai Mehta committee recommended three-tiers institutional arrangement to make people’s participation necessary. According to these recommendations the government set up PRIIs for e.g. Rajasthan and AP at first. However, Karnataka stands for classical case of decentralisation. Initially, PRIIs were not assigned specific functions besides their being elected bodies. However, compelling circumstances paved away to include PR as mandatory provision with a legal status for weaker sections, regular elections and finance commission and state finance commission under the 73\textsuperscript{rd} CA 1993.

Much later under the Chief Ministership of Shri Ramakrishna Hegde the government has given new guidance to PRI it is enacted in 1983 Act with a party based election with a two-tier elected office Mandal Panchayat and ZP. This PR experiment in Karnataka was landmark step in the development of local self-government for the rest of the country.
This prioritized the rural development through people’s participation; under this Act two statutory bodies TP Samithi at Taluk level and advisory and coordinating with no executive functions and GS was envisaged below the Mandal Panchayat. They have right to prepare and approve development. Zila Parishad was a powerful body which administrated schemes and development programmes. For the first time the elections were conducted on party lines with 25 per cent reservation for women.

The preamble Act of 1993 express the main objectives of declaration that PRIs should function as units of LSG. Even though the developmental functions were transferred to ZP much development was not seen. In Karnataka working relationship and good progress came to exist between various governmental departments and NGOs working in the areas of social forest and waste land development. NGOs concentrate on election awareness and provide technical support in all aspects such as NGO training for women candidates etc., Policies of political accommodation were included and reservation of 33 per cent for women according to the 1993 Act.

But the authors say that Vokkaligas and Lingayats as dominant social communities have played dominant role. The required inputs of PR members are lacking; this can be tuned up by capacity-building programmes. The recent developments have been establishing of Grama Sabha with sufficient functions to take measures in Panchayats such as approval of budget, programmes, development projects, selection of beneficiaries in planning proposals; and to establish Ombudsman institution in each district.

The authors have made observation that so far as PRIs are concerned adequate functions of GS and empowerment of GS form the crux of the matter; and also provision of the political and social space for emerging weaker sections and women. Social audit must be in place for GS and it should be related to awareness of policy and programmes. GP should have people’s commitment chapter, Media should work for the fundamental changes. Progressive and innovative mechanisms are implemented in strengthening PRIs in Karnataka. The authors feel that it can be said confidently that Karnataka is going in the right direction.

Abdul Aziz (2007) presents an overview of institutional situation in Karnataka. He presents a historical and critical analysis of decentralisation process in the state of Karnataka. He emphasized that Karnataka’s evolution in the realm of Panchayats is
much like a “U” shaped curve. It devolved all 29 items at local government; and
devolution has brought to the GP and TP levels. District Panchayats have been
strengthened. As per the decentralisation index Karnataka ranks as a top state
regarding devolution of powers to the local government. There is an ample proof. In
the state of Karnataka people’s participation is satisfactory. However, even in
Karnataka the author says that MPs and MLAs are plays dominant role.
While in conclusion the author has made some suggestions which are as follow:
1. To foster some degree of efficiency in decentralized planning, the process
should have proximity to the people which leads to and needs people
participation in governance and in planning process.
2. This would be of benefit for people without middle men and facilitates
more flow of funds through taxes and contribution.
Although, author says that practically it was not implemented in Karnataka the reason
for in plan formulation and implementation there is minimal people’s participation
and a lack of this in decision-making. State level elected representatives are
dominating rather than the LSG representatives. Later author suggested some action
needed to strengthen participatory governance in Karnataka:
1. The MLAs/MPs dominance should be reduced by not giving voting power.
2. In GS meeting people’s attendance should be mandatory and this has strong
influence on accountability of administrative and elected bodies.
3. Development planning approach needs to be based on integration. This could
be done by the DPC with transparency and accountability.
4. At the district level Ombudsman should be established to curb corruption.

Kripa Ananthpur (2006) in her paper titled ‘Selection by custom and Election by
Statute: interfaces in Local Governance in Karnataka’ deals with customary
Panchayats and GPs and wide differences between them. In Karnataka most important
districts like Dharwad and Mysore have been chosen as central focus areas. Among
these four villages from each district have been adopted for research purpose under
the first section, it mainly focuses on customary and informal Panchayat institutional
structure, in the section two, customary and formal Panchayat interface has been the
focus, whereas in the third section, prominent interaction between informal
customary and formal Panchayats has been explained. In this research paper author
has raised some questions on how customary Panchayats can work like as a parallel
body and influence GP activities. The paper also deals with the 73\textsuperscript{rd} Constitutional Amendment Act and recommendations and suggestions of several committees and commissions on empowerment of Gram Panchayats. Even today how far customary Panchayats can influence in local community has been drawn attention to. The customary Panchayat can influence at Grass-root level with reference to election nomination, control of community resources and Gram Panchayat members and sometimes expect customary Panchayat leaders to smoothly run development works at the local level. By this it is understood that how significant the informal and customary panchayats are. Sometimes the informal panchayats also matter in designing the beneficiary programmes in favor of village elites’ preferences.

This research study is quite related to one of our research objectives regarding local bodies to be transformed into effective units with respect to grassroots functioning. Because many times the location of roads, water tap etc. are dictated by informal customary Panchayats rather than elected Gram Panchayats. Over all, the author strongly emphasized that effective people’s participation is to be encouraged in Gram Sabha and wherever customary Panchayat dominates its influence found should neutralized. And the author financially advocates a strong and the effective local political structures at Gram Panchayat level and increase in the social movements for effective participation and also capacity-building.

**The Case of People’ Plan Campaign in Kerala:**

Thomas Isaac and Patrick Heller (2003) in their research paper titled ‘Democracy and Development’ mentioned the vibrant nature of Indian democracy and effective institutions of democracy. Authors begin with Archon Fung and Eric-Olin Wright’s exploration of participatory of governance and institutions of liberal democracy. They say that in order to address challenges of local democracy in India, the representative structures dominated by the elite interest, fears, political competition between the parties has led to unequal and fragmented social structures and these need to be addressed. In the absence of programmatic political formation this is difficult. According to their view parties such as CPI (M) are exceptions. Equal opportunity provided by the constitutional structures is scuttled by all the interest groups. This chapter charts the struggle for democratization and evolution of the key institution (Kerala state planning Board) and the process of ‘People’s Planning Campaign’ in
which both Thomas Isaac and Patrick Heller have been involved. As an institutional programme the campaign was targeted for greater participation of citizens.

The first principle was to transform local government institutions from delivery conduits for national and state schemes into full-fledged self-governing institutions with financial and administration autonomy. The devolution of functions and administration should be based on the principle of subsidiarity (what can be best done at local level should be done at that level only). The second principle of representative structure should be complemented by more direct forms of democracy. This would help improve popular participation of citizens and accountability and transparency in bureaucratic operations; the campaign designers where instrumental in making the state structures respond to the campaign. The success of land reforms of 1970s in Kerala was most significant for improving equity. The mass literacy campaign in 1991 also resulted in mobilizing in the popular initiatives in Kerala; and has developed civil society entities and put them into action.

Even after People’s Participatory Plan formulation and implementation in Kerala the line departments of the state government continued to dominate the planning and implementation of schemes, programmes that are supposed to be transferred to the local bodies. The decentralized planning adapted in Kerala was applied to all the three-tiers of local government; among which the grassroots tier Gram Panchayats start the planning process with democratic representation from the lowest level. Regional coordination is very significant. Democratic character was ensured through the involvement of elected officials and a range of citizen’s committees. Where planning as process was driven by mass movement.

In their concluding remarks, Isaac and Heller say that the civil society has been strengthened to bring previously excluded and marginal actress into the political arena. But it was difficult to sustain the momentum of local planning. But the gains may be undone quickly if the new institutions failed to deliver. Sustainability of such experiments rests on two factors: (1) financial devolution (2) reform in bureaucracy. This in turn depends on political environment; after the People’s Campaign with the change of government the campaign lost much state support.

Five years of experimentation of decentralisation in Kerala has evolved new sources of democratic authority and lessons that have great significance with lasting impact.
Collective work of ordinary citizens with the combined efforts of civil society and bodies such as Kerala Shastra Sahitya Parishad (KSSP) and Centre for Social and Environmental Studies (CSES) have brought effective changes. The campaign was oriented as a social movement. Kerala experience suggests that what was required and to some extent achieved was the synergy of efforts of state and society. According to Rashmi Sharma’s (2007) review of the idea of decentralisation through people’s plan campaign in practice in Kerala, the author provides a very unique insight into the concept of decentralisation. This state devolved the functions, functionaries and funds not only to GP but at ward level. Based on a case study of a GP she clearly defended basic needs and long term development needs. She presents the view that Panchayats have been able to address related issues regarding basic needs of the people. The remarkable step which appears in Kerala’s model is the devolution of funds at local level without overlapping other line departments and functionaries.

In 1996, Kerala state has taken a remarkable step in the form of People’s Plan Campaign at the level of grassroots including people in the planning process, resource mobilization and capacity building. Also funds devolution can be seen in this period. The author explains the implication of decentralisation, second section focused on conceptualization and implementation in planning campaign. Overall this paper explained the dynamics of Kerala Panchayats and its emerging issues.

Author explained the factors which contributed the PPCs strength and weakness; first it was the impact of 73rd and 74th CAs which provided political momentum across the country. Thus, Kerala Panchayat Act, 1994 was passed. Second and third factors were the problems of economy and the stringent Left Parties agendas; she also contends that sudden breakdown of Soviet Union led to the rethinking of the agendas of the left. At that time they did not have adequate answers to these phenomena and LSGs were in the forefront of influence of the Left Parties. These circumstances led the Left parties to adopt different development methodologies which contributed to the strengthening factors for PPC.

Author has divided PPC into four phases and she emphasized that PPC has a pioneering step for development; but when it comes to the complex phases on awareness, technical expertise, administrative and financial there were difficulties.
This resulted in weakness of PPCs. Although to fulfill this gap there was review undertaken, the process of planning continued to evolve past 1998-99. However, from empirical based author said that still there was a difficulty to get details on financial matters from the GPs regarding revenue, plans and expenditure and found corruption in this. To curb this author suggested that good and expert accounting needed.

Where people were involved very high degree of politicization has taken place and it was a hindrance for the LSGs. Author found that people are very active in plans and in identifying their needs but they lack in perspective plans. So the author claims that GPs should have more capacity to manage resources. The GPs should adopt new strategies for development; wider network of LSGs is needed. The local bodies are aware of pros and cons of the solutions in their plan projects. Overall this paper stressed professional up-gradation in the decentralized planning and expected less key role of the state.

Cases of Uttar Pradesh and Madhya Pradesh:
Ravi Shrivastava (2006) in his paper ‘Panchayats, Bureaucracy and Poverty Alleviation in Uttar Pradesh’ presents the details of 73rd Constitutional Amendment Act and the 1994 Uttar Pradesh State Act and discusses the responsibilities, functions, powers and capacities in detail. He also discusses the need for further measures for devolution. Shrivastava discusses antipoverty programmes, planning programmes and change of implementation from bureaucracy to local level democratic institutions. According to him in Uttar Pradesh this has not been fruitful; though of late more poor people have greater say in concerning these matters. Along with this he notes that 74the CAA makes DPC mandatory. With respective financial aid from the Union Finance Commission and State Finance Commission to PRIs the allocation of money is found plenty but Shrivastava notes that the allocation is not according to scheduled time table; thus crippling the entire development work. Also he has discussed the financial crisis in the state regarding delayed allocation of state matching grant in 1998-99 which affected welfare functions of PRIs. When we compared to financial resources of PRIs in the entire country UP is an exception. Here PRIs financial allocation has been gradually reduced year by year (from 1989 onwards). Although, from 1999 onwards under budgetary transaction in PRIs have maintained adequate transparency by village Panchayat. The author has remarkably
found that there is a great debate in the Gram Sabha meetings regarding allocation of grants in aid. Apart from that the knowledge of receipts and expenditure are individually known in some part of villages. In some villages the transaction, receipts and expenditure will not be known because the local secretary of the PRI has mismanaged it.

Due to the role of middlemen the implementation of poverty alleviation programmes to the local level has seriously affected. The prominent middlemen in UP being the village Pradhans, bank officials and block functionary or professionals. Due to this kind of corruption the poverty alleviation programmes are hampered miserably in the decentralized planning. However, in few villages effective implementation of public work is taking place owing to the local level committees. In this study all the ingredients (effective committees and planning) and other variables are seen to be resulting in the best out comes;

Another claim by Ravi Shrivastava was that bureaucracy also leads to corruption and that is a hindrance factor for development. Along with these factors performance of village Panchayats is varied. He has also explained the positive and negative opinions of working of PRIs:

Ravi Shrivastava has identified literacy and educational attainment; the quality of elected leadership and the quality of government and its functionaries as responsible.

In regard to this issue author has emphasized under taking certain measures:

a. Hamlet wise quorum in GP and GS meeting
b. Identification of beneficiaries, selection and preparation of schemes, project supervision, account etc should be made and strictly adhered
c. Trainings should be given to policy makers and bureaucracy
d. Priority should be given to administrative and financial supervision
e. Appointment of watch dog committees at local level is necessary instead of bureaucracy
f. Panchayat functionaries should be brought under Panchayat administrative control.

Jafari and Vikas (2006) discuss the situation of gender in PRIs in Madhya Pradesh and in their paper ‘Mainstreaming Gender in District Plans in Madhya Pradesh’
focused elaborately on the role of Madhya Pradesh district level planning process. In this authors have considered how far women are participating in planning and are involved in the planning. In Madhya Pradesh according to 243ZD District Planning Committee has been established. Therefore, urban and rural local bodies devise their own district plans effectively. But composition and selection of District Planning Committee differs from one state to other state and also Madhya Pradesh Panchayat Raj Act accords full planning power at the district level to PRIs. Similarly, Janapad, District level and village level services plan preparation and exercise will be chalked out and also roles of women’s and their decision in planning studied.

Even at the district level the functions related to plan linkages and allocation of human resources including gender related issues has been identified. Therefore, authors have clearly selected three districts and five villages in each district in this regard. Here authors have noticed the problems of lack of comprehensive planning at district level. Beside that space given by the district plan for local level planning is too ideal to be real. At the Village level only a few members and secretary were involving budgetary plan preparation without women’s participation. Plan prepared at GS will be just read out at this level. By this it’s understood that the role of secretary is very powerful. In this research paper more emphasis given to gender related and budgetary planning, but he says woman role and participation in preparation of plans and women’s concerns are not taken into consideration. According to Madhya Pradesh Panchayat Raj Evam Gram Swaraj Act 2001 an opportunity for reservation for women in GS is provided. But the level of participation is very less. But compared to the other groups SC and ST women attend more meetings but in this case also there is no effective participation in planning.

The case of West Bengal

Ghatak and Ghatak (2007) describe the functional organizational structure in PRIs system in West Bengal. In this state local self government elections are conducted once in every five years much like in all other states. Implementation of land reforms and informal money lending and class dynamics yielded power to the farmers and as a result the stake holders like farmers, peasants, sharecroppers, school teachers hold position in local governments. This paper studies the introduction of mandatory Gram Sansad meetings. Here Gram Pradhan is all powerful at local level. The authors’ feel that in today’s context Grama Sabhas have to hold powers for audit correction and
suggestions of citizens should be considered. According to this study even in the budget allocation to the Panchayats line departments still have a great role even in West Bengal.

State-wise implementation of 73\textsuperscript{rd} Constitutional Amendment: Some Selected States:

Arunachal Pradesh

Arunachal Pradesh Panchayat Raj ordinance was replaced by Panchayat Raj Bill, 1994, which was adopted by state legislature assembly. But then Governor sent this bill for President’s assent. But the bill was returned by the Centre with certain observations. The observations mentioned provisions for Gram Sabha and reservation for SCs. Later on this bill was reconsidered in the assembly in 1997 modified but rejected reservation policy for SC. Since SC population was very least again this bill was sent to president in 1997 still it has not been returned. In due course the state Governor extended the life of elected Panchayats in 1997 under NEFA Panchayat Raj Regulation Act, 1967 for two times (1995 and 1996) for a period of one year. Under 73\textsuperscript{rd} CA the original Panchayat was for three years but this amendment does not allow extension and allows them to complete normal term.

In 1997 the state government ordered the dissolution of Panchayats which have completed two years. Thus, a strange situation was created regarding the tenure of Panchayat institutions. After the introduction of specific constitutional amendment bill in 1999 in the Parliament, the state government has sought exception of SCs and STs. The relevant clause under Constitutional Amendment bill says nothing regarding the Article 243D, with reference to reservation of SCs and shall not apply to the state.

The salient features of this Act are direct election at GP level. Anchal Samiti is elected by presidents of GP. This Anchal Samiti is in place in its original level (block level). But elected members have been increased to 40. MLAs, Lok Sabha and Rajya Sabha members, Circle Officer are all the part of Anchal Samiti. But
officials will be less; whereas ZP composition remains same with MLAs and MPs without officials. ZP members elect the ZP chairman. The GP members and Zila Parishad members elect Anchal Samiti and its term was increased to five years with provision for women’s reservation. Provision is also made to have State Election Commission and State Finance Commission. These Panchayat Raj bodies have been a delegated power which comes under Eleventh Scheduled of Constitution. Necessary mechanisms for funds have been devised through grants-in-aid. State government has wide powers to override the Panchayats: suspend the Panchayat’s constituency, suspend electoral process; further state can remove the chairperson or the member at different levels if he or she found to be of undesirable conduct or acting against the public interest. These factors are problematic for the functioning of PRIs.

Assam

Act of 1992 was replaced with enactment of Assam Panchayat Raj Act, 1994, excepting the districts of Corabi, Guohonlong and North Cachar. This Act applies to all rural areas in Assam. Here also three-tiers of PRIs have been provided for according to the PR rules of 1995. Under this Gaon Panchayat (Village), Anchalik (block) and Mokkum Parishat (district level) were established. Here the rules have been framed for the conduct of Panchayat election, election of Panchayat members and DPC and reservation for SCs and STs Women. Under the rule 252 automatic dissolution of Mokkum Parishat is possible. But even after the 1994 Act Parishat elections were not held. After the new government came in 1996 it dissolved the all the rural local bodies in 1997 although, the Act clearly specifies conducting of election within six months as per the relevant provision; but state government did not conduct election so far.

This Act provides Gaon Sabha and it functions as a recommendation body and for selection of the beneficiaries. In case if this Gaon Sabha fails to identify the beneficiary within the stipulated time, the Secretary will be empowered to do this. Gaon Panchayat has no powers for appointing staff. In Anchalik Panchayats reservation has been provided. 28 functions were been enlisted to each Anchalik. This block Panchayat also has three standing committees. State government assigned functions to these bodies under this Act. Assam Government can
nominate one officer as CEO at Parishat and Chief accountant officer and chief planning officer and government can issue directions for these bodies.

**Andhra Pradesh**

With reference to Andhra Pradesh the Panchayat Raj Act 1994 was enacted on 21st April. This replaces earlier AP Gram Panchayat Act 1964 and 1986. This new Act provides three-tiers structure, that is, at the each GP, Mandal and ZP level. Under this Act Gram Sabha composes the village community and it should meet twice a year under the chairmanship of Sarpanch. Gram Sabha considers matters relating to annual statement of accounts, its report on administration and development programmes for village and taxation purposes. The GP and particularly the GS is divided into Ward Sabhas. Reservation has been given for SCs and STs based on the population and rotation. Also reservation gives BC and (33 percent) for women under the reserved category. GP headed by Sarpanch who is directly elected by voters of the GP for five years term. Reservation is there for the post of Sarpanch (for women, BCs, SCs and STs). Sarpanch controls village executive officer and village development officer. Above all commissioner of PRIs exercises control over the Gram Panchayats. This Act provides GP, beneficiary committees for GP level; and functional committees are constituted for agriculture, water, sanitation, education etc. GP also prepares annual administration reports and discharges all obligatory functions and also taxation powers. They also collect advertisement tax and professional etc. they receive grants from state government.

Mandal Parishad: this Act provides MP for each Mandal. This consists of direct elected members and also members of Lok Sabha and Rajya Sabha and Legislative Assembly and one representative from minorities. These elected members of Mandal Parishad are eligible to contest to the post of president and vice president of the Mandal Parishad. The reservation has been increased as a whole to 34 per cent. President and vice-President are reserved for SCs and STs. The functions of Mandal Parishad are community development: agriculture, fisheries, animal husbandry, infrastructure and anti poverty etc. The grants will be provided by the state and central governments.

Zila Parishad: ZP is meant for district level. This consists of elected members elected by territorial constituency. Two members are minority members one is co-opted. Chairperson of district cooperative market society, Zila library Samithi,
district cooperative, central bank, district collector and all Members of Parliament in the district are permanent invitees but do not have voting power. CEO will be responsible of resolutions because he is appointed by state government at the ZP level.

Financial powers of ZP are such as examining and approving of Mandal Parishad budgets, distributions of funds, considerations and consolidation. Decisions have to be ratified by the General Body of ZP. The ZP is also responsible for preparation of District level plans. Source of income for the ZP is central and state government grants from various bodies, local cess and state taxes.

The GPs seek prior approval of commissioner to abolish any existing tax; especially here Mandal Parishad and Zila Parishad have no powers for taxation. This Act does not provide any confidence motion against Sarpanch; because the Sarpanch is directly elected by the voters. This Act provides SFC to review financial position of PR bodies; State Election Commission is also provided under the Act to regularly conduct the elections in free and fair manner for local bodies.

Bihar
New Bihar Panchayat Raj Act, 1993, repealed the old Panchayat Raj Act, 1947, and the Bihar Panchayat Samiti and Zilla Parishat Act of 1961. This Act was passed without discussion being held in the legislature. This Act restores the same functions of Gram Sabha like budget, development programmes etc. The important aspect is report of vigilance committee. This committee is created by Gram Sabha from the outside of Gram Panchayat. This will help the Panchayat committees to act properly or discharge their functions properly. Thara or wards are given statutory status. So it acts more powerful than the Panchayat. This Act provides new population criteria for Samiti and Zilla Parishat members’ direct election for Mukhiya, members of Samitis and Parishat. Whereas indirect election to be held for blocks Pramukh and Zilla Parishat Adhyaksha (women also have reservation in this); percentages of population are taken into criteria in reservation for SCs, STs, and BCs.

This Act also provides By Laws and rules framed with approval of Zilla Parishat officials of Gramsevaka representing state government. The glaring omission in
this Act is land reform from Panchayat list. State government has wide powers to remove elected Mukhiya’s, Pramukha’s and Adhayaksha at the three-tiers. This Act clearly defines the role of ZPs as a supervisory body over the GPs. It can go to the extent of and suspending through executive order the Gram Panchayats. State government can dissolve any three-tiers of Panchayat as per section 131. The unique features of Bihar Panchayat Raj Act, 1993 are Gram Rakshadal and Gram Kacheri. In this Act these tiers come under the grip of state government and it is not allowing them to grow as local self-government units.

**Haryana**

This Act is implemented as Haryana PR Act of 1994 with a restructured modification in tune with 73rd CA, where three-tier PR system was restored. Under this Act the term of chairperson of Zilla Parishat and Panchayat Samiti are for five years. PRIs in Haryana are dominated by the MLAs and MPs who interfere much. Officials always swing to the tune of the MLAs rather than chairpersons of ZP. Many functions of Panchayats have been provided but not implemented. These institutions have no control over them.

**Madhya Pradesh**

The new Act in 1993 replaced MPPRA 1990. The new Act was passed without debate in the legislature. This Act includes the reservation, provision for GS control over DRDA, representation for SCs and STs. Grama Sabha has full powers; Sarpanch can always call a meeting. GS can discuss any matter of GP. No confidence motion of incumbents. A political decision of elected body has been subjected to executive authorities. This authority has widely misused by officially to remove from chairs.

This amendment provides that Panchayats shall have power and authorities as may be necessary to function as self-governing institutions; and have authority for selection of employees to implement schemes. This Panchayats have been given the power to deal with the 23 government departments. And later the government added many functions.

One or two functions are given for Zila Panchayat. In 1996 the government announced transfer of further powers has been given over rural health and primary education to Panchayats. The practical problems of PRIs are in case of transfers of the functions, funds and finances and programmes also powers and responsibilities over the 29 guiding items of the 11th Schedule. As an institution of
government the concept district government or Janapad Panchayat as a chief implementing agency has been enunciated. Classifications of planning for social and economic development are the main responsibility of Panchayats. In 1999 DPC were in charge of a minister, a chairperson, with the district collector as chief secretary and the DPC is only subordinate agency for government.

**Maharashtra**

In order to conform to the provision of 73rd CA Maharashtra Amended GP, Zilla Parishat and Panchayat Samithi Acts of 1958 and 1961. And it was implemented in April 1994. Under this Act following changes have been observed: reservation for all categories in GP, state election entrusted the number of seats for SCs and STs in proportion to the population. 27 per cent seats reserved for BC, 1/3 sears for women, reservation is also extended to STs and SCs at Sarpanch level; 1/3 total number offices reserved for women.

Panchayat Raj bodies enjoy special administrative powers under Maharashtra ZP Act. Necessary factor have been introduced safeguarded to balance certain provisions of PR laws; and key factors were introduced such as sanctions of powers and development schemes; powers of awarding the contract have been provided to ZP and Panchayat Samithi. There under the pattern of decentralisation administration is ensured by devolving powers by committee wise; and empowering the chairperson of each committee with the administrative powers and financial powers. Here standing committees have overriding aspect with respect to all subjects to avoid misuse of powers. Similarly ZPs have the same to amend the direction given by the president.

PRIs are involved and are responsible for execution and maintenance of development works. Overall ZP prepares long term plan, annul plan by utilizing the local resources and deals as an agency to ameliorate the conditions of poverty of the SCs and STs. Many schemes under ZP like agriculture, planning plantation, animal husbandry, rural employment etc. have been included.

This Act recommends the principle of allocation of tax, shares and grant-in-aid to local bodies. The SFC is constituted for the revival the financial status of local bodies. The government modified several recommendations.

Under this Act DPC has been constituted only to draft district development plan for a district as a whole; and guidelines to the matter concerned are given. It
consists of 33 to 55 members; ex-officio members will be ministers of in charge. Officials play very important role in this. MPs and MLAs are permanent invitees. ZP allots functions to consolidate and consider annual plan prepares. Concept of five years plan to monitor the progress of perspective plans is introduced. The government created various cadres under Zila service known as DTS. This determines the initial strength and composition of staff each intermediate Panchayat with its own staff gazetted officer, BDO. At the Village level Gram Sevak is Parishat servant assigned for GP. Here the Act provides governance through committees for greater decentralisation.

**Recommendations of Various Committees on the functioning of PRI**

**and Planning:**

Recommendations of the Rajiv Gandhi Foundation’s ‘Voices from Below: Summary Proceedings of Sub-Regional Workshops on Panchayats: Issues and Recommendations’ Under the aegis of Rajiv Gandhi Foundation various sub-regional workshops on PRIs were conducted across the country in zonal wise or state-wise. Here we are giving the broad suggestions and recommendations as they emerge from these workshops for PRIs at various levels.

Constitution and Composition: Under 73rd Constitutional Amendment Act Article 243G has not been effective implemented; because, the word ‘may’ has been used extensively and this word itself indicates a weak point in implementing the necessary changes. Instead of the word ‘may’ the word ‘shall’ must be used. Therefore, all the Central Act should be made mandatory. By this manipulation by the states can be prevented.

Apart from this there is a clash between Central Act and the State Acts. Since there is no organic link the Central Act mandatory provision was made for membership under various levels. It is also recommended the new concept of horizontal linkages between urban local bodies and PRIs. Apart from this priority should be given to the district level regarding integrated developments and the recommendations suggest removal of dual standards.
The working of DPC also is considered by the workshops. This workshop advocated common legislation and structure for all states with respective district level governance. If GS has to be strengthened these necessary powers should be allotted. With regard to devolution of powers and functions state should understand eleventh schedule and 243(G) regarding economic development and social justice in connection to PRIs. Therefore, a committee should form to study the above said issues (article and schedule). Besides that parallel institution like DRDA, WDC etc must be merged in PRIs.

In order to give more financial power to PRIs there should be power to impose independent tax and larger tax assignment and so as to increase non-tax revenues. Under eleventh scheduled list of 29 items should be transferred to PRIs. With regard to local area Development, provision should be made for district flow of MPLAD funds to PRIs and also Panchayat Finance Corporation should be established to strengthen all local bodies' development activities with regard to loan facilities. Strengthening revenue collection machinery is strengthening for high revenue collection. State finance commission should play important role. Formulation of revised devolution formula is a must.

With regard to planning and development Zila Panchayat president should be chairperson for District Planning Committee. DPC should consist of all the three-tiers’ chairpersons or presidents. DPC must have detail research survey on human and financial resources and physical geographical, infrastructural data. Holding sound data resource helps better planning process under decentralized planning. Apart from this planning and development committee should have representatives of farmers, artisans, retired personnel and senior citizens. Voluntary associations should be presented at all the tiers.

Establishment of State Development Council is necessary to coordinate and guide PRIs activities. Also PRIs have to have their own service commission for selecting their staff in the lines of U.P.S.C. With reference to this Part 14th of constitutions of India should be amended. At district level developmental functions should be given to PRIs. Chief Executive Officer of ZP should be raised to the level of Deputy
Commissioner. Elected members of PRIs should be given training on planning and accountants. PRIs should seek or involve Voluntary Organizations at the local level.

**Recommendations of Shri K. S. Krishna Swamy Committee:**

K S Krishna Swamy Committee was constituted by the Government of Karnataka in 1988 to evaluate working of Zila Parishads (ZP) and Mandal Panchayats (MP) under the chairmanship of Shri K S Krishna Swamy. This committee consisted of eminent persons like Shri P S Appu, Dr.L C Jain and the Director of Rural Development and Panchayati Raj (RDPR) Department. The main objectives of the committee were to study and make an assessment of ZP and MPs with respect to their nature of work and to identify remedial factors. Also the Committee aimed to study the administrative matters regarding devolution of powers, administration, including financial administration. The attempt was also to examine the prevailing inconsistent, relationship between ZP, MP and committee members and their relationship to the state government. Shri Krishnaswamy Committee also studied the impact on development programmes with respect to the role of Panchayat. In this view committee has identified some issues and given recommendations. Followings are the salient recommendations:

1. The members of the legislature, members of the parliament, ministers and officials of the state government have mental reservation about the scheme of decentralisation.

2. The climate of downward accountability is missing and in such climate often efforts are made to make in roads into the authority of local governments. Such a development should be strongly restricted at the political level. The committee has also expressed that there is a gross mismatch between functional responsibilities of MP and control over the resources. This trend should be changed.

3. Further there is no immediate need of Amendment to 1983 Act to guide inter governmental relationship and commitment to politically move ahead with the actualities of decentralisation.
4. So far as the functioning of Mandal Panchayats is concerned they should be strengthened; so that the GS will can come over the constraints on its functioning. Otherwise people will lose their trust in attending GS meeting as effective local authority.

5. Overall good amount of co-operation and mutual understanding of MP and the PRI representatives is necessary even in case they come from different political party. There is serious problem regarding this cooperation and linkages. Considering the role of the MLAs the chairman, Panchayat Samithi, this is considered as a healthy convention but should be limited. The practical course should be modified to improve the linkages and means of communication between MP and ZP.

6. Better arrangement can be made with reference to membership of elected representatives on rotation basis among MLAs, ZP and MP Presidents or Pradhans.

7. At present there are nine standing committees; but it should be reduce four or five groups by re-grouping the ones existing. So that more regular meetings could be held rather than once in a month.

8. With regard to budgetary support compared to Mandal Panchayat, ZP has greater authority on functions.

9. With reference to devolution of authorities to PRIs the state government should reiterate is total commitment; direct and indirect measure to reduce the authorities of ZPs and Mandal Panchayats will not be tolerated.

10. The Committee also advocated reactivating the state development council and urging the state government to conduct regular meetings of the council; and its Secretariat and responsibility for the council should be transferred to the Secretary RDPR. The procedures and convention should be modified to prevent state minister and legislature becoming overbearing with regard to day to day administration of ZPs.
11. In order to present any clash or abridgement of rights of statue of PRI's a committee headed by an outside expert in government plus officials representing state and ZP plus non-officials should be constituted by the government.

12. Practically there is a great need to work out the budgetary allocation from the government to PRI's.
13. In the process of streamlining the administrative set up at all three-tiers it should be possible to shift the sufficient number of village accountants from revenue department to provide one more functionary to each Panchayat.
14. Part time of Assistant Commissioners for human resource should be utilized for certain development duties;
15. Therefore, strengthening the planning capability should be there to suit the needs of decentralisation.

The entire Krishnaswamy report made specific suggestion to overcome the failures, shortcomings with some speed at low cost which is to be acted upon. And this would also foster area based planning approach.

**Recommendations of the Ramchandran Committee (2005):**

Ministry of Panchayat Raj set up a Task Force decided by review meeting of the Prime Minister under the chairmanship of V Ramachandran to prepare for the Eleventh Five Year Plan based on District Plans related on Part IX and IX-A of the Indian constitution. In this regard the committee focused to strengthen District Planning Committee on its composition, functions and its responsibilities and gave its expert advice and recommendation:

1. According to Article 243ZD provides for District Planning Committee to establish across the country for consideration of the Annual and Five year plans of states.
2. In this regard, state has to make law and also should take its own decision on its composition.
3. As per Article 243ZD (3) (b) DPC take technical and professionals assistance on its functions, responsibility and preference for GP and Taluk/Block
Panchayat development plans also consolidate and prepare urban and rural plan for Municipalities and Panchayat Raj Institutions.

4. Parallel bodies like DRDAs and District Health Societies need to be modified to incorporate into the DPC in the process of district level planning particularly regarding Centrally Sponsored Scheme (CSS).

5. The Planning Commission strictly informed the states that DPC is the whole and sole body for consolidating plans at the district level.

6. The Planning Commission could specify framework to states to issue detailed instructions with which DPC can perform its functions within a stipulated time.

**Recommendations of the Eleventh Five Year Plan:**

The Planning Commission emphasized that development is about desirable change in a society and best to be achieved and related to the basic needs. Best development represents equal or balanced development; but it takes place only when resource utilisation is proper. This proper utilisation only happens when integrated planning made from bottom-up approach such as planning formulation at the grass-roots level. In India Central Schemes were made at top level although they are effective at grass-roots level. But commission stated that these schemes should be restuctured according to the needs. in this regard different tiers of PRIs have responsibility to full fill their assignments in planning and implementation: The specific recommendations are:

1. co-operation, co-ordination and harmonization of existing planning and implementation arrangements and institutions with the Panchayat Raj set up

2. Increase in allocation of funds to different level of tiers

3. Need to provide technical support for plan formulation and in implementation

To take care of these above said issues the commission emphasized that decentralized planning follow up these steps:

1. Gram Sabha and Self Help Groups get assessment and priority based setting with participatory and network

2. With the help of participatory Rapid Appraisal Techniques the local resource should be analysis with simple methods.

3. Effective local level participation with stakeholders and experts could be involved while in formulation of local development at various tiers.
4. There should be need based project assessment and situational analysis by expert working group at different levels of PRI's and consolidate of development proposals of the working groups. Also there should be detailed project reports.

5. Prioritization of proposals and allocation of resources to the prioritized proposals

6. Vetting of project reports on technical and financial aspects by technical Advisory Groups of DPC

7. Consolidation PRI's plans into District Plans; and clarity in the plan prepared by the DPC.

8. To develop sectoral and cross-sectoral, different tiers plans; and these should be merged into one district plan. Priority should be given for grassroots level. For this discussion and dialogues could be arranged; some essential factors involved in this process are:
   a. DPC should be strengthened in its functions and act as full-fledged institution rather than a committee
   b. At the district level DPC interact with research institutions and academic institutions and are encouraged to improve and establish resource network.
   c. DPC could be assisted by Technical Advisory Groups and different sectors as well as from civil society.
   d. The Planning Commission issues common guidelines for plan formulation with line ministries.
   e. Relating to district plan the state governments should issue brief guidelines towards decentralized planning within the framework stipulated in the report of the expert group.
   f. To provide information at least from the block level from time to time to generate a local statistical system by increasing the sample size of national sample survey.
   g. There should be expert institution identified for state development report at the district level and for pilot district plan should be entrusted to that institution.
The Expert Group committee on Eleventh Five Year Plan emphasized that DPC should be established as a separate and permanent office with adequate secretariat to service it at the district level. But it should not emerge as another layer of bureaucracy and as a substitute to people’s plan.

It also identified the current status of DPC and observed the unequal composition of members and functions etc across the country. It also identified that most of the states never consolidated nor activated on district plans.

**Recommendations of the National Institute for Rural Development (NIRD):**

The NIRD, Hyderabad made some observation and recommendation on the existing Panchayat Raj system in various major states in India— in all about ten states—these are related to our research we have taken some of the recommendations. They are as follow:

1) As per the 74th CAA DPC are to be constituted expeditiously. This will also provide an opportunity to have appropriate representation in the committees and in getting local plans, schemes programmes etc. this could result in suitable action for district plan. For e.g. Madhya Pradesh constituted the DPC under a separate Act *Madhya Pradesh Zila Yojana Samiti Adhiniyam, 1995*. This is helping in decentralized planning at the district, block and Village level.

2) To make inter-tier linkages between three-tiers and this helps in co-ordination while in finalizing the plan for district as a whole. Whereas Balwant Rai Mehta Committee suggested that to hold an organic linkage between three-tiers there should be a blue print for local level bodies

3) There is lack in devolution of powers and functions. However, few states have implemented but in reality there is no effective implementation. To fulfill this, states have to take some necessary account for administrative set up because in India the administrative set up, resource and financial set up differ from states to states. In Karnataka the Act it self has spelled out the powers and functions to take decentralisation forward.

4) The State Finance Commissions are almost all states have established. So that states have to take necessary advice of commission on budgetary, schemes, programmes and under Eleventh Schedule of constitution which must be transferred to PRIs. Also transfer of staff associated with these subjects towards Panchayat Raj bodies.
5) According to Article 243(G) PRIs have to take responsibility to prepare development plans and implementation; to keeping in view ‘economic development and social justice’. So there should be strict and proper guidelines and manuals. These things could be widely circulated in different levels of PRIs including functionaries to Panchayats and public. This would be representing broad aspects of local level plan and on the other hand awareness of PRIs powers, resource etc.

6) At the block level Taluks or Panchayat Samitis have to be given priority as main units of planning. In few states its proximity to the people and also availability of technical and non-technical staff (For e.g. Karnataka.). Once given priority at block level which will meet the objectives of constitutional mandate under Article 243 (G). Because these bodies have some primary responsibility of planning and co-ordination. Because in India villages have yet to be equipped in respect of well trained staff, technical and professional etc.

**Recommendations of the Expert working group committee of Karnataka:**

1. Create mass Capacity-Building and it can lead decentralisation movement. While a sustainable system has to be devised and people should know the changes. Also this committee feels that must have feedback and monitoring system on their action.

2. Committee realized that there should be Vasathi Sabha--a body consisting of persons registered in the electoral rolls of each Panchayat member’s constituency at ward level within the GP. Vasathi Sabha is proposed to be more intense and meaningful for people’s participation. Here committee says requirement of quorum is also necessary.

3. If Panchayat members practice continuing absence in meeting his or her membership could be disallowed as a Panchayat member. In this regard it is suggested that among the sub-clauses 13(1) A, B and C, the clause C could be changed.

4. While calling the Panchayat meeting the intimation period towards GP members proposed to be increased to ten and three days respectively for ordinary and special meetings.
5. It is proposed that attending the meetings by officers needs to be made ‘mandatory’ rather than ‘entitled’.

6. Certain activities relating to making contribution at GP level prior approval stipulation from TP should be removed. And GPs President and Vice-President become executive heads of the GP and having control over the GPs staff relating to call for records, pass orders and do suspension within the boundary of law.

7. To take infrastructure developments at the GP level prior approval of TP is to be removed as same ZPs prior approval to TP is also removed. Also the same in respect to budget.

8. The committee argued that to avoid political dominance in TP ex-officio membership (MLAs/MPs) is to be removed also in the other elected bodies.

9. The working group members supported the concept to establish Ombudsman with different functions towards PRIs. And dissolve GP power entrust to government through this institution rather than TP and ZP.

10. Each tier needed freedom in their plan to send directly to DPC.

11. At the State Panchayat Council, TPs and GPs Presidents and Vice-Presidents should get represented.
Chapter -3
Planning and Budgeting in Tumkur district

In Tumkur district the District Planning Committee – DPC-- was constituted only 2007-2008. So far no meeting of the DPC has been held. The reasons for not holding DPC meetings are DPC comprises rural and urban local bodies and some times election to some of these local bodies is not held and full DPC body is not formed. According to district level officials this is the reason for not having held the meeting of DPC. The reason is unless the full body of DPC is present the meetings can not be held. However, at present the full body of DPC is exists and the Zila Panchayat officials say that the meeting of DPC will be held at any time now.

In this district planning is done according to the following diagram

![District planning diagram]

The district level planning according to above figure takes place in two ways. The 1st is general planning or statutory planning that the local elected bodies are supposed to undertake. This general planning is done largely through tied funds. The other plan existing in the district called Grama Swaraj Plan. Gram Swaraj Plan is supported by the World Bank it provides untied funds to Grama Panchayats.

It is interesting to note that DPC is virtually non-functioning in the district though here is planning process going on at all three tiers of Panchayat Raj system. The general planning is done bottom up from gram Panchayat level to ZP level; whereas in the case of Gram Swaraj Planning, planning is done from ward Sabha level of gram Panchayat up to TP level and from TP level Gram Swaraj Plan go directly to state level; without the intermediation of Zila Panchayat level. Politics and conflicts of interest take place in the planning process when there is ambiguity among the three tiers of the Panchayat system. In such case allotment of funds is a problem because the priorities the three tiers of local government or different
Plan integration

Plan integration is important both from horizontal point of view and the vertical point of view. From the point of view of the integration of the urban and rural plans as well. The integration of urban and rural plans does not exist at the present in the district. The rural plans are prepared by the Panchayati Raj department whereas the urban plans are prepared by the Deputy Commissioner or Collectors office at the district level. Therefore the integration of plans for rural local bodies and urban local bodies does not exist at present.

Detailed discussion with district level Zila Panchayat officials show that the plans are prepared at the TP and ZP levels by bureaucrats; and all of these officials are on deputations to the planning department. The involvement of the elected representatives is there at the GP and TP levels but not much at the district level. And these officials who prepare plans too are not properly trained in the planning process. The district officials expressed concern about this fact. Many of the planning officials at TP and ZP levels are on deputation from departments such as horticulture animal husbandry or agriculture department; some of the officials are also from rural development department. These officials do not have any training or capacity building in the planning process. The ZP level officials expressed their view that there should be separate and trained cadre for planning purposes at all levels for both rural planning and urban planning and for meaningful integration of both.

When enquired whether any conflict exists between the state government and the local bodies the district level officials felt that there is sufficient role clarity between the two and conflicts are rare

Devolution Process

Funds

So far as the devolution process is concerned, as our village studies show there is sufficient devolution of funds in this district. There is also sufficient devolution of functions. According to the Karnataka Panchayati Raj Act of 1993 all the functions in the 11th Schedule are devolved to PRI system. The problem mainly is with the functionaries. Functionaries are not devolved and they still continue to function either from the line departments or on deputation to PRIs and urban local bodies.
In the release of funds as far as housing goes the State and Central governments are releasing money directly to panchayats. The same is the case with the Grama Swaraj plan. In Gram Swaraj Plan, assisted by the World Bank, also the funds are released directly to GPs in untied manner. The money goes directly to the villages in the case of these two whereas in certain cases ZP has to release finances. These are statutory funds and the routine aspects such as maintenance of water supply, drainage and other such schemes.

The district level officials hold that the PRI Act of 1993 is the guideline according to which the PRI act functions are devolved line departments. But they candidly affirm that in spite of the Act the control over functions and functionaries are with the Zila Panchayat. They say that both ‘budgetary and administrative control is with ZP’.

The situation was better in the late eighties and early nineties when an IAS officer senior to the rank of that of District Collector was the ‘chief secretary’ of the ZP and the PRI system enjoyed much freedom and authority and the PRI system was stronger. Now the situation has worsened. Finally, so far as the devolution process is concerned the situation of Tumkur Taluk and that of Karnataka shows that the finances and functions are devolved without sufficient devolution of functionaries.

**Developmental Profile of Tumkur District**

**Basic Demographic details of Tumkur district and sample Taluks**

The Tumkur district total population is 5,16,661. Among them 2,68,341 are gents, 2,48,341 are ladies; 2, 67, 732 people are staying in rural areas, 2,48,929 people are staying in urban areas. The density per Sq kms 504; sex ratio is 925. Out of 33 taluks we have chosen Kunegal, Thiptur and Gubbi taluks.

The Tumkur district total rural scheduled caste population is 55,414. Among these 28,276 are gents and 27,138 are ladies. And the total urban; most of the scheduled caste people are staying in rural areas. The Kunegal total rural scheduled caste total population is 27,436. Among these 13,380 are gents and 14,056 are ladies. Thiptur total rural scheduled caste population is 25, 406. Among these 12,620 are gents and
12,786 are ladies. And the total urban scheduled caste population is 5078. Among these 2596 are gents and 2482 are ladies. So the scheduled caste urban population rate is very high compared to rest of two taluks. The Gubbi total rural scheduled caste is 38,780. Among these 19,659 are gents and 19,121 are ladies and total urban scheduled caste population is 2122. Among these 1068 are gents and 1054 are ladies. So the Gubbi urban scheduled caste population is very low compared to rest of two taluks.

The Tumkur district total rural scheduled tribe population is 19,641. Among these 10116 are gents and 9,525 are ladies and total urban scheduled tribe population is 9,512 among these 4944 are gents and 4,568 are ladies. So the total scheduled tribe population is very low compared to scheduled caste population. More details are provided in the statistical annexure.

**Literacy rates in Tumkur:**

The Tumkur district in 2001 the literacy rate is 75 percent. The Gubbi taluk the literacy rate is 67.5 percent. The Kunegal Taluka literacy rate in now is 61.3 percent. Totally, the Kunegal taluk literacy rate is low compared to our other two sample taluks. Thiptur taluk literacy rate is very good; the literacy rate at 75 percent is equal to Tumkur district literacy rate.

The Tumkur district rural literacy is 66.7 percent among them 76.8 percent are gents and 55.8 percent ladies, urban area literacy rate is 83.8 percent among them 88.1 percent are gents and 79.1 percent are ladies. In Totally the urban literacy rate is high compared to rural areas. In Gubbi taluk rural literacy rate is 66.4 percent ;75.8 percent for gents and 56.7 percent for ladies; urban literacy rate is 84.1 percent among them 89.2 percent for gents and 79.4 for ladies. The Kunegal taluk total literacy rate is 61.3 percent among them 72 is of gents and 51 percent of ladies. The rural literacy rate is 58.8 percent among them 70.1 for gents and 48 percent for
women; urban literacy rate is 78.6 percent among them 84.3 percent is of gents and 72.5 is of ladies. The Thiptur taluk total literacy rate is 75 percent among them 83.7 percent is of gents and 66.2 percent that of ladies. The rural area literacy rate is 72.5 percent; among them 82.4 percent are gents and 62.5 are ladies; and urban literacy rate is 82.9 percent among them 87.8 are gents and 77.7 percent are ladies. All in all, the entire literacy rate is high in urban areas; and the male literacy rate is high among all taluks.

Source: - Tumkur district at a glance

**Chart – 1**

**Taluka wise Sex Ratio in Tumkur District**

The district statistics (provided in the annexure) show Taluk wise sex ratio of Tumkur district. The high sex ratio is in Kunegal and Turuvekere is equal i.e. thousand female for thousand males sex ratio. And rest of all Taluks has average sex ratio. Among these Tumkur has low sex ratio compared to other Taluks.
The details of health institutions in Tumkur district are provided here and in table format in the annexure. In Tumkur district we have chosen three Sample Taluks are Gubbi, Kunegal and Thiptur. In Tumkur district there are 7 health centers are there, among these in our sample Taluks only two health centers are there one is in Gubbi and another one is Kunegal Taluk. And allopathy dispensaries only one is in Thiptur Taluk and Indian system of medicine centers one is in Gubbi Taluk and another in is in Thiptur Taluk. In Gubbi Taluk 2 main and 57 sub family welfare centers are there, in Kunegal Taluk 3 main and 41 sub welfare centers are there, in Thiptur Taluk 5 main and 42 sub welfare centers are there, there are 54 drug shops in Gubbi Taluk, in Kunegal Taluk 44 drug shops, and Thiptur Taluk 74 drug shops are there. And there are no blood banks in Gubbi, Kunegal and Thiptur only one blood bank in Tumkur.

**The health institutions in Tumkur district:**

The details of health institutions of Tumkur district are dealt with in the following for the district *in toto* as well as for three sample Taluks details. In Gubbi and Kunegal Taluks there are no allopathy hospitals, in Thiptur Taluk one center is there this center
has 50 beds capacity. There are 5 Indian systems of medicine hospitals in Gubbi, and each center has one bed capacity. In Kunegal Taluk only one center is there and in Thiptur Taluk 6 centers are there and its capacity is 10 beds. There are 3 private hospital are in Gubbi and these hospital capacity is 6 beds, in Kunegal Taluk 1 private hospital is there and its capacity is 15 beds, in Thiptur Taluk 12 private hospital are there and these hospitals capacity is 112 beds. Primary Health centers in Gubbi Taluk 11 are there and its capacity is 78 beds, and there are 7 health units in Gubbi and its capacity is 4 beds. There are 10 health centers in Kunegal and its capacity is 72 beds. And there are 8 health units in Kunegal and its capacity is 8 beds. In Thiptur 8 health centers are there and its capacity is 42 beds. And 4 health units in Thiptur and its capacity is 4 beds.

The lower primary education in Tumkur:

The details of lower primary education are dealt with here (the same are provided in table format in the annexure). These are provided for Tumkur district, as well as for the three sample Taluks details. In Gubbi Taluk total 263 lower schools in Gubbi among these 254 Government lower primary schools are there among these 9774 are boys and 9465 are girls. And only one aided lower primary school in Gubbi which this 489 are boys and 284 are girls, in Gubbi eight un-aided schools are there among these 943 are boys and 999 are girls. In Kunegal Taluk 300 lower primary schools are there among these 290 Government lower primary schools among these, 8439 are boys and 8471 are girls. No aided school in Kunegal and 10 un-aided lower primary schools among these 1584 are boys and 1242 are girls.

The situation of higher primary education in Tumkur:

The details of higher primary schools in Tumkur district, as well as three sample Taluks details show that in Gubbi Taluk total 168 schools are there among these 4826
are boys and 4406 are girls. Among these schools 150 government schools among these 4168 are boys and 3841 are girls, and 9 Aided schools are there among these 357 are boys and 254 are girls. There are 9 un-aided schools among these 301 are boys and 311 are girls. In Kunegal Taluk total 158 higher primary schools are there among these 5146 are boys and 4986 are girls. Among these 133 Government schools among these 3533 are boys and 3439 are girls, and 10 Aided schools are there among these 1147 are boys and 1211 are girls. There are 15 un-aided schools are there among these 466 are boys and 336 are girls. In Thiptur Taluk total 131 higher primary schools are there among these 4118 are boys 3936 are girls. Among these 101 Government schools among these 2610 are boys and 2616 are girls, and 7 aided schools are there among these 929 are boys and 687 are girls. There are 23 un-aided schools are there among these 579 are boys and 633 are girls.

The statistics concerning the other aspects of high school education, pre-university education, rain fall and other aspects of the district profile are provided in tabular form in the Statistical annexure.

With this basic statistical profile regarding human development and introduction of the district we proceed to examine the situation at Taluk and GP levels.
**3-1: Planning process at taluk level**

**Gubbi Taluk**

*Geography*

Gubbi is one of the taluks of Tumkur district; it is 20 Kms from Tumkur town. Gubbi is located at 13.31, 76.94 latitude and longitude. It has an average elevation of 767 meters (2516 feet). As of 2001 India census, Gubbi had a population of 16,802. Males constitute 51 percent of the population and females 49 percent. Gubbi has an average literacy rate of 76 percent, higher than the national average of 59.5 percent; male literacy is 80 percent and female literacy is 71 percent. In Gubbi, 11 percent of the population is under 6 years of age. Gubbi has 33 Grama Panchayats.

In this taluk there are 33 Grama Panchayats. From out of 33 Grama Panchayats we have taken three sample Grama panchayats, these Grama panchayats are: Changavi, Heruru and Thyagatur. As per Nanjundappa report Gubbi is designated as most backward taluk, and following this consideration government appointed a Taluk planning officer at Gubbi in order to improve planning process at Taluk level and also at Grama Panchayat level. In the following we first discuss the situation for Gubbi at taluk level, following that we discuss the planning process in three Grama Panchayats: Thyagatur, Changavi and Heruru. All three Grama Panchayats represent various levels of development in Gubbi Taluk.

In Gubbi taluk planning process is taking place in relatively better manner compared to other Taluks. In this planning process all officers, Taluk Panchayat president, vice president and members co-operating to prepare plans; they have information constraint, but in spite of this, planning is taking place relatively well. District planning committee is interacting with taluk Panchayat. Grama Panchayats are submitting their plans to taluk Panchayat before they take up plans for action; the government has a set of guidelines; if the plans are as per guidelines they consider otherwise the Taluk Panchayat is again correcting the plans and then the plans are revised. Then Taluk Panchayat is submitting all G P plans to Zila Panchayat.

In Gubbi taluk following schemes are implemented:
1. 12th finance plans
2. Stamp duty collection plans for resource generation
3. Grama swaraj plan
4. Nanjundappa Report
5. Ashraya Ambedkar Yojana
6. Taluk action plan
7. Indira Avas Yojana
8. Suvarna Grama Yojana

**Taluk action plan:** In preparing the taluk action plan the steps are: first ZP asks Taluk Panchayat to prepare plans and is providing guidelines. Then taluk panchayats prepare plans as per guidelines. After that they are discussed in Taluk Panchayat general body meeting and then submitted to ZP. If these plans are passed by ZP, then they call engineers for tender for giving work order. There are different plans prepared for different schemes and they are as follow:

**Ashraya Ambedkar Yojana**
According to officials this plan is implemented since 2003. The finances under this plan go directly to Grama Panchayat. For the years 2005-2006, 2006-2007 this Yojana has been implemented and for 2007-2008 the Yojana was not prepared; and presently, 2008-2009 it is in process.
As per Nanjundappa report under the Ashraya Ambedkar Yojana 35 houses are granted for each Grama Panchayat.

**Suvarna Grama Yojana**
Under this scheme the Grama Panchayats and Taluk Panchayats are providing computer training to rural unemployed students.

**Meetings**
- Taluk Panchayat general body meeting – Monthly once
- Taluk officers meeting (KDP) – Monthly twice
- G P secretaries meeting- Monthly twice
- Quarterly with MLA KDP meeting

An interview with the Gubbi taluk executive officer shows that there are two different plans implemented in the Taluk; firstly the general planning as per the constitution
and secondly, the Grama Swaraj Plan initiated by the World Bank. He gave more information about Grama swaraj plan. As per Nanjundappa Report since 2006-2007 the Grama Swaraj Plan is implemented in Karnataka in 39 taluks. In Gubbi taluk also the Grama swaraj plan is implemented in 33 Grama Panchayats. Grama swaraj plan differs from the general plan. Grama Swaraj has its own rules and regulations to prepare plan. Grama Swaraj plan is being implemented at Grama Panchayat and village level only. This World Bank funded plan is a five year plan. The Grama Panchayats getting certain amount yearly. The amount per year is minimum of six lakhs and maximum of 10 lakhs.

The Grama swaraj plan was prepared and implemented for the years 2006-2007, 2007-2008, and 2008-2009 plan is under process. According to the Taluk officials it is a transparent plan with focus being laid on accountability and transparency. In this plan people are participating in planning process with their focus being laid on basic needs like 1. Drinking water supply 2. Drainages 3. Sanitation 4. Internal and approach roads 5. Buildings (Anganavadi building, schools, school compounds)

**The Planning process**

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Ward Sabha
↓
Grama Sabha
↓
Grama Panchayat Meeting
↓
Grama Swaraj Wing (Controlled by RDPR)
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According to the guidelines of Grama Swaraj Plan, the Grama swaraj plan funds should not be used for following works.

1. Temples
2. Church
3. Arch
4. Any specific person or caste
Prior to preparing the Grama Swaraj plan the Grama Panchayat conducts a broad survey of priority issues and attempts to identify the main needs of the people. The Grama Swaraj plans are prepared as per the people’s needs and priorities. The main deference between general plan and Grama Swaraj Plan is that in Grama Swaraj Plan they are calling for tenders for all works reducing the chance to indulge in corruption. The general planning process has some scope for corruption.

**Mainly the Grama Swaraj Plan consists of three types of priorities:-**

1. Value addition to social sector services :- Education, Health
2. Focus on creating productive assets: - Health, school compounds, Grama Panchayat buildings, Anganavadi Buildings.
3. Improving connectivity: - Through roads, tank bunds etc.

**There are some parallel bodies to Grama Panchayats in Gubbi and these are:-**

1. SDMC—School Development and Monitoring Committee (in all Grama Panchayats)
2. Watershed committee/Sujala committee (in all Grama Panchayats)
3. Joint forest committee (In Grama Panchayats of Belavatha, Doda, Gunni and Marashetty halli)
4. Village monitoring committee (Any Grama Panchayat member is president of this committee)
5. Village health committee (Grama Panchayat president is president of this committee)

According to the constitution only the Grama Panchayats can generate funds and not Taluk Panchayats or Grama Panchayats. The usual sources for revenue collection by Grama Panchayats are as follow:

- Current tax resources
- Untied funds
- Total existing funds from all plans

**Gubbi taluk Planning officials:** We had an elaborate interview with the taluk planning officer in Gubbi. He came six months ago and he told that so far as planning is concerned not much involvement of Taluk Planning Officer is there. The plans prepared at Grama Panchayat level through Ward Sabha. Wherein the Grama Panchayat secretary provides information to Grama Panchayat about
government plans and schemes; the Grama Panchayat secretary also informs Grama Panchayat about the rules and regulations. The same are then discussed in ward Sabha and Grama Sabha meeting; and then the plan proposal prepared in the previous two meetings is discussed in general body meeting. The general body meets and approves the plan and then the plan is forwarded to Taluk Panchayat office. General body consists of all elected ward members, president and vice president of the Grama Panchayat and the secretary of the Grama Panchayat. All the plans are prepared in Grama Sabha and the Grama Sabha meets yearly twice. The approval of Grama Sabha is final in all cases. In ward Sabha they mainly discuss about all schemes, people’s priorities like internal and approach roads, drainages, sanitation facilities, schools and so on. The funds from local tax revenues as well as government funds are used for fulfilling these needs.

The plans of Grama Panchayat are sent to Taluk Panchayat after the approval of the general body meeting consisting of 15-20 elected members. The Taluk Panchayat then integrates the plans. The general plans thus integrated are sent to ZP for further approval and the World Bank funded Grama Swaraj plans are directly sent to the ministry of Rural Development and Panchayati Raj at the state level. In Grama Swaraj Plans the plans prepared by Grama Sabha are final and the Taluk Panchayat’s role is largely that of ensuring the process and after that the plans are sent directly to the state government skipping the district level Zila Panchayat.

The role of the Taluk Panchayat is largely that of the integration of plans in the above mentioned manner. Different sectoral plans are prepared by Grama Sabha level and approved by general body, and then they are forwarded to Taluk Panchayat. Taluk Panchayat considers the plan, either sends the plan to upper tiers or to the concerned line Departments, if it concern they forward to line Departments otherwise they forward to ZP office.

**The Urban Planning** : Gubbi is a Taluk town and has a municipal council. There is also planning for this municipal council. The Gubbi Urban Local Body (ULB) is one of the ten ULBs in the district. Interestingly there is no connection between the rural planning and urban planning. Urban plans are prepared by the municipal
council and sent to the Deputy Commissioner’s Office in Tumkur. From there the plans are sent to the Directorate of Municipal Administration in Bangalore. Therefore there is no connection between the plans, programmes and schemes prepared for municipal administration or urban governance and rural governance this is despite the fact that Taluk Panchayat Office is very much situated in the Taluk town.

The municipal planning process in Gubbi involves proposals discussion at ward level and plan preparation municipal level and discussion in the general body consisting of elected members of the municipality. After that the plan is discussed and then it is forward to Deputy Commissioner’s office. There is no plan integration at taluk level of urban and rural plans. But according to the taluk planning officer, there is need for integration of urban and rural plans at taluk level; and they have to be integrated. So that there is a single consolidated plan for the taluk. In Gubbi urban and rural plans are not integrated at taluk level. Municipalities undertake urban planning and directly send the plans to DC’s office whereas rural planning involves overseeing by Taluk Panchayat and Taluk Panchayat forwards the rural plans to ZP office. There is no integration of plans in taluk level.

In Gubbi taluk there are parallel bodies to ULBs as well. These are institutions not created newly but have been working for long time.

- APMC (Agriculture product and marketing committee)
- TAPCMS(Taluk Agriculture Product Co –operative Marketing Samithi)
- On an average there are 25 line Departments; dealing with different sectors at taluk level.

Grama Swaraj plan is implemented at district level since five years; the plan period is 2006-07 to 2010-2011. In terms of planning processes both general plan and Grama swaraj plan have separate processes, while the general district plan is prepared and sent to Zila Panchayat the Grama swaraj plan is directly forwarded to Rural Development and Panchayati Raj (RDPR) through Taluk Panchayat. There is a
special cell monitoring the Grama Swaraj plan in the Rural Development and Panchayati Raj department at the state level.

In the following we discuss the situation of planning in three Grama Panchayats, Thyagatur, Heruru and Changavi respectively.

**I. Thyagatur Grama Panchayat**

Thyagatur is one of the Grama Panchayats of Gubbi taluk; it is 15 kms from the Gubbi town. Thyagatur Grama Panchayat total population is 7483, of these 3681 are men, 3802 are women and total voters are 5000, literacy rate is 70 percent. This Grama Panchayat has 13 villages in that 6 revenue villages and 7 sub villages, six wards are there. The president and vice president are of younger age group i.e., below 40 years.

According to the Grama Panchayat secretary they have planned 10 schemes for this term, and they are planning for each scheme separately. To provide an example the Grama Panchayat has planned for the following schemes:

- SGRY (Suvarna Grama Rojgar Yojana)
- NREGA (National Rural Employment Guarantee Act)
- Ashraya Ambedkar Yojana
- IAY (Indira Awas Yojana)
- Angavikala Ashraya Yojana

First plans for the above are prepared in ward Sabha; in this meeting they discuss about plans, government schemes, rules and regulations about funds. The GRAMA PANCHAYAT secretary provides information about what are the works completed and what are the works that are to be completed. The ward Sabha considers people’s needs and priorities. And then they discuss in Grama Sabha and they finalize plans here, the Grama Sabha is held near Grama Panchayat office. Once the plan is passed by the Grama Sabha the general body of the Grama Panchayat discusses these plans. But once the decisions are taken in Grama Sabha the general body meeting does not make any amends in the plans, because they do not have any rights to make changes. The general body reviews the plans and takes care of the administrative matters and takes care of the aspects such as reservations for SC and ST communities, women and handicapped. Following that the Grama Panchayat forwards the plan to Taluk Panchayat office. If the plans are as per the rules and guidelines they accept otherwise.
they ask for a review. Totally the ward Sabha and Grama Sabha finalize all the Grama Panchayat plans.

The general body means elected members plus the Grama Panchayat secretary: The general body meets 12 times in a year i.e., monthly once, with proper prior notice. Prior to the general body meeting they give notice to all members before seven days about the meeting, time and agenda regarding the issues to be discussed. Grama Sabha meets 2 times in year, Ward Sabha meets 2 times in a year.

Grama swaraj plan is 5 years World Bank assisted plan, they prepare plan for 5 years, and as part of these they prepare plans every year as per the needs and priorities of the people. They prepare plans for all 5 years and they first discuss these in ward Sabha and then Grama Sabha and they take approval for 5 years plan from taluk Panchayat. And then they prepare plans for every year. Both 5 year and one year plans are discussed in ward Sabha and Grama Sabha and are approved by the Grama Panchayat. The Grama Panchayat Secretary assists at all stages of the plan preparation

The process of Grama swaraj planning is much transparent, with less chance for corruption; because for all civil works tenders are called for and this is done regularly every year. Those who compete for tenders and taking up works, prior to the work they have to pay 2.5 percent EMD (Earned money deposit), Tender-Less Amount and FSD (Further Security Deposit) These three funds Grama Panchayat returns after 3 months after the work completion. In between if the work damages or some thing happens, they won’t get back the above three funds; instead of them using these three funds for correcting the work damages, in Grama Panchayat resumes every work in order to complete them and in a maximum time of two years. The same safeguards and provisions are not present in general planning. And this leads to lack of transparency and accountability in general planning.

In Thyagatur Panchayat there are three standing committees working. Each committee should have 5 members in that one SC one ST candidate should be there and 33% reservation for women. The three committees are:

1. Production committee (It belongs to agriculture Grama Panchayat president is president for this committee)
2. Social justice committee (It deals with problems related to SC and ST communities and village Vice president is president for this committee)
3. Facilities committee (President presides over this committee)

Table - 17
Thyagatur Grama Panchayat members, caste-wise

<table>
<thead>
<tr>
<th>Caste</th>
<th>Members</th>
</tr>
</thead>
<tbody>
<tr>
<td>General</td>
<td>6</td>
</tr>
<tr>
<td>OBC</td>
<td>8</td>
</tr>
<tr>
<td>Women</td>
<td>8</td>
</tr>
<tr>
<td>SC</td>
<td>4</td>
</tr>
<tr>
<td>ST</td>
<td>1</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>17</strong></td>
</tr>
<tr>
<td>President</td>
<td>1</td>
</tr>
<tr>
<td><strong>Grand total</strong></td>
<td><strong>17+2=19</strong></td>
</tr>
</tbody>
</table>

Source: Thyagatur Grama Panchayat

The Grama Panchayat general body meets 12 times in a year; Grama Sabha 2 times in a year; Ward Sabha 2 times in a year.
Parallel bodies and such institutions in Thyagatur Panchayat are:
SDMC; Watershed committee; SHGs (100);

Table-18
Grama Swaraj funds to Thyagaturu Panchayat, year-wise

<table>
<thead>
<tr>
<th>Year</th>
<th>Amount in lakhs</th>
</tr>
</thead>
<tbody>
<tr>
<td>2006-2007</td>
<td>5.14</td>
</tr>
<tr>
<td>2007-2008</td>
<td>6.85</td>
</tr>
<tr>
<td>2008-2009</td>
<td>8.56</td>
</tr>
</tbody>
</table>
Every year February last week or March first week the planning process is held and the Grama Panchayat discusses about Grama swaraj plan. The Grama Panchayat secretary has more responsibilities in Grama swaraj plan. In ‘general plan’ they are considering local resources as well as needs but Grama swaraj plan they are not using local resources. In this Grama Panchayat they collect only two taxes house tax and water tax. Total Grama Panchayat own potential revenue is 7 lakhs but out of the total they collect only 50 percent. In general plan they consider people’s needs and local resources; but in general planning they are also bent more on civil works and some times they build permanent property for Grama Panchayat such as commercial buildings etc, which will help in augmenting revenues in the long run. Thyagatur Grama Panchayat office is a concrete building equipped with one computer and computer operator; the computer operator is paid Rupees 2000 per month.

In the Thyagatur Panchayat people’s main needs are often the basic ones that any average village in India requires: street lights; housing; sanitation; roads; community hall; hospitals and veterinary hospital. In this Grama Panchayat all line department officials attend ward Sabha and Grama Sabha meetings.

2. Heruru Grama Panchayat

Heruru is one of the Grama Panchayats of Gubbi taluk; it is 3 kms from Gubbi. The Heruru total population 8,142; in that women are 4013 and men are 4129. Literacy Total is 70 percent for ladies 68 percent and for gents 70 percent. It has five revenue villages and three sub villages. In this Grama Panchayat six wards are there and this Grama Panchayat president and vice president posts are unreserved.

According to the village secretary in Grama Sabha meeting 100-110 members are usually present and in ward Sabha is attended by 30-40 members. General body means president, Vice president, members; and also concerned engineers; general
body meets 12 times in a year i.e., monthly once. Ward Sabha, Grama Sabha meet yearly two times.

The planning process starts from ward Sabha level and it discusses plan in Grama Sabha and they finalize the plan in Grama Panchayat general body meeting, then they forward the plan to Taluk Panchayat. But it is the Grama Sabha that has the power of finalizing plans. Plan prepared and approved by Grama Sabha is final.

There are three standing committees in Heruru. In standing committee membership 30% is reserved for ladies and 30% is reserved for SC and ST.

The committees are:
1. Civil justice committee
2. Fundamental facilities committee
3. Sthahi committee

There are five parallel institutions working in Heruru Grama Panchayat. As per secretary those institutions do not involve in the work of Grama Panchayat. They are working separately. But some times SHG members are attending ward Sabha and Grama Sabha meetings for getting some facilities from Grama Panchayat. Some times the Grama Panchayat is inviting line Departments to attend Grama Sabha and ward Sabha meetings.

The parallel institutions operating at the level of Grama Panchayat are:
1. Watershed committee
2. SDMC
3. SHGs
4. Water users association
5. Joint forest committee

In Heruru Grama Panchayat Grama swaraj plan is there, and is happening properly. They prepare Grama swaraj for five years; this five year plan they discuss with ward Sabha and Grama Sabha. And as part of the plan they take some plans every year these plans also are discussed in ward Sabha and Grama Sabha. Then they discuss in Grama Panchayat general body meeting after that they send the plan to taluk Panchayat. In Grama swaraj plan they are getting an amount per year minimum 6 Lakhs and maximum 10 Lakhs According to Grama swaraj plan they have to complete the work within the time. The previous 2006-2007, 2007-2008 plans are
successfully completed and 2008-2009 is in process. In Grama swaraj plan they are giving information to people about schemes that are planned and implemented to people then them considering which are the needs and priorities. In Heruru Grama Panchayat, in general planning they consider all priorities as well as resources and apply for money for gaps between resources and priorities.

In Heruru Grama Panchayat they have 3 lakhs tax availability but they are collecting only 50-60% of that, they are collecting water tax, house tax and so on. The secretary told that the General Planning funds and Grama swaraj scheme funds should not be used for Church, Community hall, temple, and building arch or for any particular caste or person.

As per secretary Heruru Grama Panchayat people the needs mostly are:

1. Drinking water
2. Sanitation
3. Drainage
4. Roads
5. Street lights

The main problem is drinking water; the Government funds are not enough for drinking water needs. When they are not fulfilling people’s needs, they are not getting taxes properly and of all plans housing plan are the main problem.

The Taluk Panchayat office accepts all plans that are as per guidelines, if it they are, they will give suggestions to correct the plans. As per president and vice president the planning first starts in ward Sabha, in this they enquire about people’s needs and priorities and discuss about these needs with local members. And they consider certain needs; after that they discuss about these needs in Grama Sabha, in the Grama Sabha meeting they provide information about what are the works that have been done and what are the very urgent and essential needs, works for which funds are spent.

Before the Grama Sabha meeting, they give information to all villager and all SHG members. In Grama Sabha meeting they discuss about all plans and also finalize the plans. One -draw back is as per vice president is that in Grama Sabha meeting only the
local people i.e., from villages near to Grama Panchayat are attending; some times the attendance from distant villages is scanty.

After that they discuss the plans in Grama Panchayat general body meeting. In this meeting they do not change any plans, but some times if some needs are urgent such as water pipelining or motor service, then they take up those works.

As per president and vice president for the Grama swaraj plan they are planning for five years and they undertaking some planning’s yearly as per people’s needs. The president and vice president told that this scheme is very appropriate and good scheme because in this there is no chance for corruption because all civil works undertaken call for due tender process.

Within the Grama Panchayat some committees are constituted there but these committees not working properly. In planning process they are considering people’s needs but they give 50 percent preference to people’s needs, and they give 50 percent to local elected member’s suggestions.

In general plan and Grama swaraj plan as per vice president they only mention people’s needs and priorities, they will not mention local resources. In Grama swaraj scheme the works undertaken are: roads, drainage, pipeline for drinking water, small water tanks, and small bridges. They are not facing any problems for getting approval for planning’s from Taluk Panchayat but that plans should be as per guidelines.

**III Changavi Grama Panchayat**

Changavi is one of the Grama Panchayats of Gubbi taluk. This Grama Panchayat is 30 kms from Gubbi taluk. Changavi Grama Panchayat total population is 4857. It has seven main villages’ fifteen sub villages, and five wards.

Table -19

<table>
<thead>
<tr>
<th>No</th>
<th>Schemes Name</th>
<th>Amount and houses</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>State Government fund (Muktha nidhi)</td>
<td>6 Lakhs</td>
</tr>
<tr>
<td>2</td>
<td>12th finance</td>
<td>3,16,900</td>
</tr>
<tr>
<td>3</td>
<td>SGSY</td>
<td>1,27,624</td>
</tr>
<tr>
<td>4</td>
<td>NRWS (Drinking water scheme)</td>
<td>35,819</td>
</tr>
<tr>
<td></td>
<td>Project/Programme</td>
<td>Year/Expenditure</td>
</tr>
<tr>
<td>---</td>
<td>-----------------------------------------------</td>
<td>------------------</td>
</tr>
<tr>
<td>5</td>
<td>Nirmala yijana (Sanitation)</td>
<td>20,694 (target)</td>
</tr>
<tr>
<td>6</td>
<td>Grama swaraj</td>
<td>2006-2007-6 Lakhs</td>
</tr>
<tr>
<td></td>
<td></td>
<td>2007-2008-6.50 Lakhs</td>
</tr>
<tr>
<td></td>
<td></td>
<td>2008-2009-3 Lakhs (first term)</td>
</tr>
<tr>
<td>7</td>
<td>PMGY</td>
<td>1,12,297</td>
</tr>
<tr>
<td>8</td>
<td>Indira avas yojana</td>
<td>30 houses</td>
</tr>
<tr>
<td>9</td>
<td>Adult education</td>
<td>18,364</td>
</tr>
<tr>
<td>10</td>
<td>Self tax (Own home tax)</td>
<td>2,00,000</td>
</tr>
<tr>
<td>11</td>
<td>Ashraya vasathi</td>
<td>60 houses</td>
</tr>
<tr>
<td>12</td>
<td>Ambedkar vasathi yojane</td>
<td>20 houses</td>
</tr>
<tr>
<td>13</td>
<td>Grama Panchayat Library</td>
<td>25 thousand per year</td>
</tr>
<tr>
<td>14</td>
<td>Jaivika anila development plan</td>
<td>5,00,000</td>
</tr>
<tr>
<td>15</td>
<td>Udyoga khathri Yojana (NREGS)</td>
<td>435 members 82 rupees per day</td>
</tr>
</tbody>
</table>

Source: Grama Panchayat of Changavi

There is no problem in taking approval for plans in Taluk Panchayat but that plans should be as per guidelines. They are collecting funds from state government and some taxes like taxes on fisheries resources and house taxes from peoples. Actually they have 3 Lakhs availability of total resources per year but they are collecting only 2 Lakhs per year.

They are preparing all plans from ward Sabha level; while preparing plans they are facing some problems from the people.

**The planning process**

```
Ward Sabha
    ↓
Grama Sabha
    ↓
Grama Panchayat (General body meeting)
```

There are three standing committees that in the Grama Panchayat

1. Production committee
2. Civil justice committee
3. Health and hygiene committee

These committee members are all elected members; civil justice committee president is Grama Panchayat vice president. Grama Sabha meets 2 times in a year; ward Sabha
meets two times in a year, Grama Panchayat General Body meets 12 times in a year
(Monthly Once)

In Changavi there are three parallel bodies to Grama Panchayat
1.  SDMC
2.  Watershed committee
3.  Joint forest committee

In general planning they discuss available resources as well as priorities needs and apply for money for the resources gaps between own resources and priorities. They prepare one plan for 5 years and it includes all schemes, while preparing plans they go through guidelines. There are guidelines for planning at Grama Panchayat level. Then they send all plans every year separately to Taluk Panchayat. The plan funds can not be used for church, temple, arch or any particular person and caste. In Changavi people’s main needs are village sanitation; high school; ration cards and old age pensions.

In Changavi children’s Grama Sabha is there six hundred children up to 15 years of age represent in children’s Grama Sabha. The elected members of Grama Sabha have the authority of electing SDMC and mid day meals staff. In Changavi Grama Panchayat some line Departments participate in Grama Panchayat works. Some times line Departments Send information and reports to Grama Panchayat, and some times line Departments officers attend Grama Panchayat meetings and give necessary suggestions.

The line Departments are working according to some steps while dealing with Grama Panchayat. First is people’s voice about their needs in ward Sabha, after that they consider these needs, and find out to which department these needs are related to; and then they call officers to attend the ward or Grama Sabha meeting; in which meeting they will give necessary details and suggestions.
3-2: Planning in Kunegal taluk

Kunegal

Geography

Kunegal is located at 13.02. It has an average elevation of 773 meters (2536 feet). It is situated on the National Highway 48 connecting Nelamangala and Mangalore. As of 2001 India census, Kunegal had a population of 30,291. Males constitute 51 percent of the population and females 49 percent. Kunegal has an average literacy rate of 69 percent higher than the national average of 59.5 percent. Male literacy is 74 percent, and female literacy is 64 percent. In Kunegal, 12 percent of the population is under 6 years of age.

We have conducted detailed discussion with taluk planning officials and concern officials at Grama Panchayat level. The taluk planning officials said that the planning is done for four types of financial resources:

1) the 12th finance commission funds
2) the Grama swaraj finances at 2,43,00,000 up to each year for period of 5 years approximately in Kunegal taluk all 36 Grama Panchayat’s in the taluk receive 40,00,000 per Panchayat for all 5 years
3) the 3rd source of finances of development grants which are statutory grants from the state government of six lakhs per year Grama Panchayat these are also untied grants
4) the 4th source of finances is local taxes
5) the fifth source of finances are provided under NREGA

The taluk level officials express the untied funding more helpful; for Grama Panchayat’s between Grama swaraj and general planning there is a considerable difference in implementation. Grama Swaraj Planning is closing monitor by the world bank the ward Sabha Grama Sabha Grama Panchayat meetings the accounts of civil works and all the papers concerning these or closely monitor by the world bank.
When asked about the capacity of planning officials at Taluk Panchayat and Grama Panchayat levels the taluk planning officials felt that there is a strong necessity for training and planning for the officials working in Kunegal taluk.

Much like in all other taluks, taluk panchayats have no role work at all in the urban planning. Kunegal town is a municipal council and its planning administration is done by the municipal council which reports to the DC’S office in Tumkur which in turn reports to directorates of municipal administration in state secretariat Bangalore. This is dispute the fact that the Taluk Panchayat office is very much located in Kunegal town.

In this taluk we have taken three Grama Panchayat’s for study they are: Yediyur Nademavinapura; Hiliyuru Durga these three Grama Panchayat’s are situated in different distances from Kunegal nademavinapura is situated in 8 kilometers radius from Kunegal Yediyur is situated 18 kms from Kunegal and Hiliyuru Durga is situated remotely 24 kms from Kunegal town all 3 Grama Panchayats but purposively selected following suggestion of the taluk planning officer.

**Yediyur Grama Panchayat**

**Case Study of Dalit Elected Representative**

**Saraswathiyaamma**

Saraswathiyaamma is an SC member of Yediyur Grama Panchayat she has studied up to seventh standard and her caste is scheduled caste (SC). According to Saraswathiyaamma Grama Panchayat general body meets once in two months and Grama Sabha meets monthly once and there is no ward Sabha. Grama Sabha discusses about plans schemes and other funds and government rules and regulations about plans and the considers peoples needs and priorities.

She does not attend any Grama Sabha meetings and she attends only Grama Panchayat general body meetings; but her husband attends Grama Sabha meetings and she does not know much about planning process. But she said that they are getting all basic facilities from Grama Panchayat like street lights, drainage, roads and drinking water. She said that Grama Sabha is well publicized in the Grama Panchayat and said that before conducting the Grama Sabha meetings they distribute pamphlets to all local citizens about Grama Sabha besides arranging for a tom-tomming about Grama Sabha.
Case Study-2

Ward Member – Soubhagyamma

Soubhagyamma is one of the members of Yadiyur Grama Panchayat and her caste is scheduled tribes (ST). According to Soubhagyamma Grama Sabha meets monthly once. Grama Panchayat general body too meets monthly once, she told that she does not attend Grama Sabha meetings because they are not giving opportunity for her voice and they give preference only for people and upper caste people’s voice such as Lingayats and Vokkaligas.

The Grama Sabha meeting is attended by 20 to 25 members. She attends only Grama Panchayat general body meeting, in this meeting they discuss about people’s needs and priorities; but they do not inform about other schemes and government funds. She that ward Sabha meetings her held but she does not attend any of them. She said that in this Grama Panchayat has total of 19 villages and 20 ward members. She mainly said that Grama Panchayat secretary is not working properly and he does not tell about any schemes and funds and does not provide information to lady members. She strongly felt that there could be corruption in the Grama Panchayat and that is why the Secretary and other elected officials do not reveal the schemes and programmes. In this Grama Panchayat and much like in all the Panchayats that we have examined, Grama Sabha is held around 10 to 11 o clock in the day time; as per the law the Grama Sabha should have to held in the evening time particularly during non-working hours.

Nademavinapura Grama Panchayat:

Nademavinapura total population is 5650 and consists of 5 revenue villages and 16 hamlet villages. Among total ward members there is only one SC member is and only one ST member. The vice- president of the village is a Muslim woman. In this GP Grama Sabha meets yearly two times and Grama Panchayat general body meets monthly once. In this Grama Panchayat Grama Swaraj Plan is under implementation. We were told that planning process starts from Grama Panchayat general body meeting and then ward Sabha here they consider and collect people’s needs and priorities and give information about schemes plans and funds. They discuss about planning in Grama Sabha and almost all finalize the plan in Grama Sabha meeting. Following which they discuss the plan in Grama Panchayat general body meeting.
The Grama Panchayats have 3.5 lakhs tax availability out of these they collect 70 percent, these taxes are house tax and water tax.

According to one ward member the line department officials do not attend Grama Sabha meetings this makes it difficult for them to get information on different departmental schemes; this ward member informed that only Taluk Planning Officer attends the Grama Sabha meeting.

Following our discussion with the local ward member we visited the Dalit colony of the village and interviewed a Dalit person called Muniswamiah. He gave a very positive picture of the Grama Panchayat, Grama Sabha and ward Sabha. He said the meetings are held regularly and he attends all the Grama Sabha meetings and asks regarding some facilities in Grama Sabha like house drainages and drinking water and other such basic necessities. He said that 70% of Dalit colony people attend Grama Sabha meetings in Grama Sabha and ward Sabha meetings ordinary citizens’ voice counts.

According to Muniswamaiah Grama Panchayat provide all facilities in good manner the facilities are drainages drinking water street light in this colony some SHG’S groups are there this group ladies members attending Grama Sabha and ward Sabha meetings

**Huliyurdurga**

Huliyurdurga is one of the sample villages of kunigal taluk it is 22 kms from taluk head quarter this Grama Panchayat total population is 8895; and literacy rate is 73.76 percent. The GP has three revenue villages Hiliyuru Durga, lakkshettypura, kamplapura and hamlet villages are anathanahalli, belurupalya, krishnappanpallya. It has total 23 ward members among these there is one ST candidate and one SC candidate. There are eight general candidates 12 OBC members.
The Grama Panchayat has the below schemes:

1. NREGA
2. 12th finance
3. Grama Swaraj Plan
4. Swarna Grama yojana

They prepare plan for each scheme separately and send these plans to Taluk Panchayat separately.

Under the Grama Swaraj Plan the funds classification year wise is provided below:

<table>
<thead>
<tr>
<th>Year</th>
<th>Funds (lakhs)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2006-2007</td>
<td>6</td>
</tr>
<tr>
<td>2007-2008</td>
<td>8</td>
</tr>
<tr>
<td>2008-2009</td>
<td>10</td>
</tr>
<tr>
<td>2009-2010</td>
<td>8</td>
</tr>
<tr>
<td>2010-2011</td>
<td>6</td>
</tr>
</tbody>
</table>

The secretary told that planning process starts from ward Sabha. At ward Sabha they elicit information about people’s needs and priorities through soliciting applications; and they give information about government rules and regulations. They inform about schemes, plans and funds; then they discuss in Grama Sabha meeting and finalize the plan. Then they discuss the plan in Grama Panchayat general body meeting and send the plan to Taluk Panchayat. According to the secretary Grama Panchayat general body means president, vice-president, and all elected members.

Grama Sabha meeting is attended by 200-250 members and ward Sabha meetings attended by 50-60 members; some line department officials attend Grama Sabha meetings. Grama Sabha and ward Sabha meet yearly twice and The Grama Sabha general body meets monthly once.

In this Grama Panchayat there are three standing committees but these committees are not working. The committees are

1. social justice committee
2. production committee
3. village monitoring committee

The Grama Panchayat has Rupees 9, 59,000 of own tax availability. Out of this availability they are collection only 65-70 percent.
The Hiliyuru Durga people’s main needs are
1. Drinking water
2. Drainage
3. Sanitation
4. Internal and approach Roads
5. Street lights

Much like in Gubbi Taluk the Kunegal taluk experience also tells that planning through ward Sabha is happening regularly and this is what is interesting. In the district while the DPC is dysfunctional and does not meet, the Grama Panchayats follow the system of planning through conducting ward Sabha and gram Sabha. The best practices in planning seem to take place at the bottom of the PRI system and not at the top i.e., at the Zila level.

In Kunegal taluk also, which is one of the most backward taluks of the district, the interface between the rural planning and urban planning does not take place. Kunegal taluk town where the Kunegal Taluk Panchayat Office is situated is a shanty town. The civic amenities in the town are non-existent and the municipal council does not take care of sanitation and hygiene. There is a strong need for collaborative planning between rural bodies and urban bodies at the Taluk level and Kunegal town which looks like an urban slum, makes ample case for this integration in planning and budgeting.
3.3. Local level Planning Process at Thiptur Taluk

Introduction
Before looking into the plan process of local level bodies the structure of Thiptur Taluk Panchayat (TP) needs to be considered. For any successful implementation of plan the staff or human resource is important. Presently, in TP there is 27 members of staff, including Executive Officer (EO). It is observed that there is a vacancy for Taluk Planning Officer (TPO) which has not been filled. According to Executive Officer, Taluk Planning Officer will be appointed preferably for ‘most backward’ regions. Despite the absence of TPO the planning process of Thiptur TP goes on as per the schedule. The overall responsibility of planning is that of EO. Besides the staff, TP General Body (GB) has 17 members. According to EO the GB of Taluk Panchayat works well with the staff. Any plan at the local level will be brought before the GB for meaningful debate. The EO informs all the GB members in advance regarding planning initiated at that level. The members will be informed about special meeting before seven days and ordinary meeting before ten days. In this regard around 18 to 20 line departments come under their jurisdiction.

Plan Implementation at Taluk Level through TP
The plans at the Taluk level pertain to:
1. 12th Finance Commission (FC)
2. Samarthy (to empower villages and people)
3. Stamp Duty (SD)
4. Action Plan (AP)
5. Ashraya (for housing)
6. Navagram (for housing)
7. Indira Awas Yojana (IAY)
8. Ambedkar (for housing)
9. Matsyashrya (for housing)
10. Nekar (for housing)
11. Handicaps (for housing)
12. Semi-migration (for housing)
13. S.G.S.Y.
14. S.G.R.Y.
15. N.R.E.G.A.

16. Special Component Plan (SCP and TCP)
The plan is prepared for all the above schemes. In the plan a few schemes in particular villages are omitted (for e.g. Navagram, S.G.R.Y.). In the housing sector beneficiaries like semi-migrants, fisherman, weavers etc. according to their demands are to be provided. For this reason the implementation of this scheme is moving slowly and less number of targets are achieved.

12th Finance Commission: This is related to budgetary allocation. Under this planning the following aspects are covered: a) rural markets, b) developing basic infrastructure, c) agriculture marketing and management (APMC), d) weekly markets, e) development of marketing place and f) management, g) providing computer desk facilities, h) supply of sports equipment to Panchayats; i) lab equipment for primary and secondary government schools, j) buildings of Anganavadi institutions, k) computerization of TP office, l) and creation of database and account management.

Samarthya: This scheme is jointly funded by the World Bank (WB) and matching grant from the state government of Karnataka (GoK). A sum of Rupees 26.10 lakhs has been allotted for the development of villages under this scheme. The state will share 16.00 lakhs and remaining amount will be shared by the WB.

Stamp Duty: Revenue earned by the TP through stamp duty has been utilized according to the plan programmes. This is an untied fund. But its percentage of or sharing of revenue is less this year, that is, 0.5 per cent (approximately 2.00 lakhs) compared to the past years which accounted for 3 per cent total revenue.

Special Component Plan: Under this plan housing facilities has been provided for SC communities, whereas roads and drainage facilities are provided for Tribal people.

Action Plan: TP has its own action plan in the General Body of the TP where they discuss all the development activities of taluk Panchayat and proposals which come before the TP will be elaborately discussed at an approved in the meeting. After that the action plan will be designed and sent to Zila Panchayat (ZP). If ZP wishes to see that there is a need for minor changes in the developmental proposals in the form of action plan the ZP will return to TP for reconsidering or remodifying. If in case the TP is
adamant and sticks to its action plan then ZP has full power to reject those plans. This might happen in cases where the action plans are not according to guidelines and which propose more expenditure.

**Karnataka Development Plan:** For implementation of this plan the elected representative or the respective MLA will be the chairman. A quarterly meeting will be convened with all the heads of the line department at taluk level and it will presided by the MLA to discuss developmental activities of the taluk. Also, there is lot of scope to implement the integration of the plan programme but this is not yet to be done because of the lack of coordination among various departmental heads at the taluk level.

**Budget:** At present TP will get around 3 to 4.5 lakhs from untied funds of the state government. This fund has been effectively utilized to bear all the expenditure incurred at the Taluk level for various purposes which is mentioned below:

<table>
<thead>
<tr>
<th>Expenditure on</th>
<th>Amount (P.M.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Petrol</td>
<td>16,000</td>
</tr>
<tr>
<td>Power</td>
<td>6,000</td>
</tr>
<tr>
<td>Phone</td>
<td>2,000</td>
</tr>
<tr>
<td>Stationery</td>
<td>2,000</td>
</tr>
<tr>
<td>Others</td>
<td>30,000</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>56,000</strong></td>
</tr>
</tbody>
</table>

According to EO sometimes power bill will not be paid in time to Karnataka Electricity Board by TP; inspection work is also hindered because of less allocation of untied funds by the state. Quarterly incurred expenditure of field visit Travel Allowance bill sent to the ZP also is reported to be not reimbursed in time. This ultimately affects the work culture at the grass-roots level. Even though, for the first time Comprehensive District Development Plan was asked by ZP for all taluks and Thiptur taluk was the first Taluk to submit the same to ZP.

**Taluk Panchayat and District Planning Committee (DPC)**

At the outset we came to know that DPC meeting has not been held according to EO and City Municipal Council (CMC) President. In their view the DPC was only namesake institution. And even most of the GPs secretaries said that they have not
heard about DPC even though they have the Panchayat Raj handbook. By this we observed that the effective work of DPC is not taking place. Although we have learnt that there is a progressive development that the DPC as it is now has come forward for the plan preparation. There is also a hindrance when the DPC asks to submit 50 copies of plan preparation from TPs; owing to the shortage in a stationery allocation, TPs will delay in submission. Despite all the difficulties Thiptur TP has mobilized Rs. 5,000 from each of its Gram Panchayats and contributed to ZP/DPC. The TP however does not know where the amount contributed went to: whether to the ZP or to the DPC. But we have been told that this amount went to ZP and along with this contribution plan prepared was sent to the ZP;

**Preparation of Plans**

**Taluk Panchayat and Gram Panchayat**

Based on tied and untied funds the whole planning process is being designed and initiated after discussion by concerned elected bodies, GP officials and the EO. Before finalizing the plan at GP level, a meeting is conveyed at GS to receive all the proposals from the villagers regarding planning process and regarding the allocation of targeted funds at the GP level. But the power to sanction untied funds will finally rests with the General Body at the GP level. For this better coordination is required between GB and secretary of GP.

**Ward Sabha and Gram Sabha**

A meeting is conveyed with respective ward members of GP to take up the people’s problem and redress them. Proposals of all the untied funds will be decided in the General Body of the GP. But in order to spend allocated tied funds for all its proposals it should be brought before GS and GB for discussion, framework, design module of plan regarding tied funds and send it to TP. TP makes minor changes, and again it will be sent for final approval to ZP. In this Taluk it is said that the meetings of Ward Sabha are conducted less than once in a year and gradually it loses its importance over time.

In Grama Sabha the problems of the Panchayat such as housing and other related plans and identification of beneficiaries are discussed. Besides that water, power and health and other related problems are also discussed.
Nonavinakere Gram Panchayat

Nonavinakere GP comes under the category of ‘developed’ GP. This GP composes of three main villages and two hamlet villages. The GP consists of 19 elected members with woman as its president. There is a staff of ten members including secretary. According to GP secretary there are two standing committees: Social Justice Committee and purchasing committee. It has comes to our notice that these committees are not functional.

Under this GP jurisdiction the following plan has been initiated such as:

1) 11th Finance Commission
2) Ashraya
3) Indira Awas Yojana
4) Ambedkar Awas Yojana
5) P.M.G.R.Y
6) Navagram Yojana
7) Mathsyashraya Yojana

Action Plan

About the Action Plan formulation of this GP around Rupees 2.00 lakhs will be estimated for road repairs, removal of waste from the drainage and repairing hand pumps etc. Recently this GP was awarded prize for keeping its village clean on count of number toilets existence in the villages under the scheme of Sampurna Nirmlyan Andolan Yojana. The awarded fund Rs. 7.00 lakhs is being used for used for construction purposes.

Usually the GP collects the taxes which are imposed on house, transfer of home deeds, shops, business establishments, general license, advertisement, market and commodities and village fairs. All the three GPs are trying to get the main source of income by constructing business establishments and letting them on rent. As per GPs sources around 4 to 7 lakhs is the total revenue and around 75 to 80 per cent of taxes will be collected. The income received by tax imposed will be used for various purposes like laying down the streetlights, road repair, repairing the bore wells etc.

GP and untied Funds (state)

All GPs gets 5.00 lakhs as untied funds. Each GP will spend 60 per cent of untied funds to pay electric/power bill. Therefore, ZP (because it was discussed and criticised at state level) issued a circular to all the GPs to drastically control the power bill. And it intimates that meters should be used, streetlights have been properly
managed, leakages of power in mini tank should be control and rectifying of mini
tanks for all the above-mentioned reasons GPs must take a whole of it.

General Problems at GP
In all the three GPs Honnavalli, Maththihalli facing major problem in drinking water.
In Honnavalli two ponds/lakes was been dried up because of drought. Where as in
Maththihalli lack of power supply in mini water tanks and regular break down of bore
wells due to the power problem. Besides that fluoride contents are present in water in
this GP limit. Because bore well are deep dug (500-800). This has resulted to raise
many diseases. Even though the GP has tested it properly.

Hurdles arising out of planning implementation and process

1) Lack of co-ordination between GB and Secretary
2) Most of the developmental works are carrying through GP members
   without monitoring and enquiry. This resulted substandard work at GP
   level.
3) The members spend most of the GB meeting to ensure that their sitting
   fees is released at the earliest without any deal
4) There is no specific plan program
5) There is no proper mechanism distribution of tied and untied funds for
   take up the development programmes because members always fight
   to distribute the sanction amount among themselves to take up the
   development works which again incomplete. This hindering whole
   development process.

Honnavalli Gram Panchayat

Honnavalli GP is one among the Hobli in Tiptur Taluk. It includes six villages which
are Kanchagarnahalli, Kerebandipalya, Hospattanna, Thippepalya and Krishnapur and
this village come under non-hamlet. There are three wards; first and second ward
reserved for ST and SC respectively. Honnavalli GP consists of 15 elected
representatives (6 were woman) called as General Body of GP. There are two bill
collectors, one peon, 2 watermen, one paurkarmika (scavenger) and one secretary.
There are 3 standing committees or sthayi committees which are looking some
particular issues in their jurisdiction called as:

1. Social Justice committee
2. Production committee  
3. Purchasing committee and  
4. Vasathi committee  

According to GB members they have not met the above said committee meeting and these issues will generally discussing in the GB meeting held where monthly meeting goes on.  

According to GB members and secretary these are the following schemes being implemented:  

1. Nirmaly Grameena Yojan  
2. Action Plan  
3. 11th and 12th Finance Commission  
4. N.R.E.G.S.  
5. S.G.S.Y.  
6. Swatchch Gram Yojan  
7. Navagram Yojan  
8. Ambedkar  
9. Indira Awas  
10. Ashrya yojane (for handicapped)  

Has been implemented but some of the plans will implementing like N.R.E.G.S. grants which is allotted but the implementation has not yet to taken. Because of works was not entrusted to GP. In the S.G.S.Y. planning they are uplifting the BPL families they are helping to get bank loan for their self-employee especially to SHGs.  

Planning Process  

We have already discussed in the beginning stage that WS are only on GP document according to their elected bodies. But GS meeting is taking place as per rules from last two years they have conducted 6 GS because of scarcity of Drinking water and some extent it was solved at present people are getting in a week. This shows that GS meets according to people’s needs and their problems.  

After discussing in GS they will prepare a minute and again they will discuss at Panchayat meeting (GB and secretary). We have been told that there were 3 types of meeting one is emergency meeting which could be informed to GB within 24 hrs, special meeting at least 3 days and ordinary meeting will meet after prior notice-
7 days. However, in most of the GS meeting discussed on selection of beneficiaries, Drinking water facilities, street lights etc. but lack discussing in education, health (source: GS minute books).

However, planning process is much liberalized not only this GP most of the Thiptur GPs are model for this type; although they are not crossing the rules and guidelines.

Mobilizing resources: this GP mobilizing its own resource from its own buildings rent. This account will goes to its untied fund. And they are utilizing on some developmental works on roads repairs etc.

Facilities given through GP: Building for BCM hostel, E.P.F fund for check dam, driving license for SC and ST.

**Maththihalli Gram Panchayat**

Maththihalli will come developing GP and it is a Kasaba (those villages comes adjacent or near to town) village consists of 10 villages, 12 sub-villages and 2 non-hamlets. The total staff of GP is 15 including secretary. 24 elected representatives representing as GPs General Body in Maththihalli. GPs GB consists in the age group of 27 to below 40 years this could be advantages while in plan formulation because they are very enthusiastically participating in the GPs every meeting (but excluding women).

There are 7 major plans have been implemented as follows:

1. 11th Finance Commission
2. N.R.E.G.S
3. N.R.W.S(state)
4. Swachch Gram Yojan
5. Navagram Yojan
6. Indira Awas Yojan
7. Ashraya

Planning process: there are similarities in planning process from one GP to other GPs in Thiptur especially in untied fund But sometimes it differs from the coordination between secretaries and General Body. This result will make their GP to hold a popular state at Taluk level.
The Role of Elected Representatives in Planning Process

The participation role in the elected representative is to implement developmental programmes like roads, drainage, drinking water, lights and identifying of the beneficiaries of all the schemes. Members expressed that the perspective plan at GP level could not be implemented according fixed time; because of exigency problems. When they were asked about its significance they say it does not mean the GPs will not take up perspective plans. But in Tiptur most of the GPs have built building and also put up various pharm related business for e.g. Billigiri, Honnavalli, Dasarighatta and Nonavinakere etc.

Planning Process

As per theoretical and secondary source the GP members who themselves are local have a regular contact with the people their problems effectively address and taken up in GP meetings and solution will readdress. Practically the mechanism towards public redressal grievances is not effectively handled by GP members at grass-roots level, although they will identify the needs of the people and device the schemes to implement it. Then it will send to TP and ZP according to the set guidelines for the final approval.

The summary of entire planning process at GS and GB meeting with approval duly sent to TP after thorough modification and design. This will be followed again with some minor changes at TP level. Sometimes when there is loophole in the plan the plan again goes to GP. After that GP will make changes according TP guidelines and returns it to TP for final approval.

People’s Participation in Planning Process

During our field study it has come to our notice that the local people will take up their problems to be addressed at the GP level through GS meeting. Although, the redressal of public problems and their needs not so effectively done for e.g. drinking water and irrigation water problem has not addressing from the past 10 to 15 years at Honnavalli GP; even though this problem brought in every GS and GP meeting. The reason is negligence by concerned authorities and lack of effective people’s participation. However, presently the people at local level are well aware about the schemes through debate and criticism. In addition to that we felt that there should be good coordination
between the GP officials, elected members for the wider implementation of the developmental programmes.

**Negligence of Local Bodies making in Effective Plan Implementation**

**Lack of Leadership**

In Tiptur TP under the scheme of plan programmes called TRYSEM most of the local people registered to undergo training in tailoring conducted by concerned authorities at district level. The beneficiaries of TRYSEM is identifies by TP( under this plan programme scheme beneficiaries there care certain condition to be followed; transportation charges followed by concerned beneficiary to undergo training programme. According to the executive officer even though mass public by drive has been done to avail training for tailoring and others under TRYSEM responses of them are very poor. As per EO ‘s experience he said that Gauramma who is member of (Stree Shakti) SHGs of Honnavalli GP had come forward to take up tailoring programme only in her GP level but there programme take place only at designated at district level with all the infrastructure. But Gauramma was not interested to go at the district level for a training programme because long distance and want to bear transportation charges o here own. But in case of NREGS this Grauramma promised to take up under this programme to mobilise people within a week she forgotten take leadership because she could not succeed there fore she withdrew from participation. The biggest problem which we found here how to motivate the people at the local level planned programmes like NREGS and TRYSEM. Here which we found was even though there was genuine demand for tailoring but it was a greater burden to GP or TP.

**Corruption in Plan implementation**

If we want to mention a case where money has been drawn to a same tank under different names without completion it is classical e.g. how the total rupees 89,000/- has been drawn under different names by GP level of Kurbarakatte, which is near to Nonavinakere. Here we found that money has been misutilised for the same work (silt) which is only existed on paper but not completed. Even though local of Nonavinakere and GP aware about corruption they are not raised this issue at al. this is greatest hindrance for effective plan implementation.

**Lack of Effective Plan Implementation**
During our field study when we interacted with the concerned secretary of GP level regarding the mode of selection of true beneficiaries housing of physically handicapped is not in a order. There was classical case where physically handicapped people get certified from the doctor that they are 75 per cent to 80 per cent only to get the benefit. During our study the genuine beneficiaries are devoid in the local level for e.g. in Matthihalli. But this kind of attitude will not be set right by the concerned the secretaries even though they were familiar about loopholes to identify the beneficiary.

**Urban Local Body Planning in Thiptur: The Thiptur City Municipal Council**

In 1927 the Municipal Council (MC) was established recently this MC was evolved as City Municipal Council (CMC) in 2007. This CMC composes commissioner and its staff and 31 members of Council Body (CB). There are regular meeting held every month but without Ward Sabha meeting. The CMC gets grants and funds from various sources as follow:

1. **12th Finance Commission**
2. **State Finance Commission**
3. **SFC Special Grants**
4. **Untied Funds**
5. **Municipal Funds**

**Programmes being conducted at CMC level**

1. S.J.S.R.Y
2. Nagar Mazoori Udyoga
3. D.W.A.C.R.A

Apart from this there is a World Bank project on Under Ground Drainage System which will soon be initiated. In this up-gradation of slums, installation of overhead tank and water treatment will be done. This project expenditure is released through a nodal agency at the state level. In addition to that the funds contributed from MLA and MP Local Area Development funds are being used.

**Planning process**

Whether planning proposals has to be initiate it will take up in CB and discussed thoroughly later the plan proposal/design will sent to the Deputy Commissioner (DC) office/District Administration. Again Deputy Commissioner will put stamp of approval if it is technical; or if it is town planning he will send that to (District Urban Development Council)DUDC for verification of technical aspects and necessary
changes according to guidelines. After the approval from DUDC it will be sent to DC and then it will be sent back to City Municipal Council with resource allocation to carry out the task. Even though the DUDC returns the plan proposals with the instruction of necessary changes and modifications the CB, the latter flatly refuses it and strongly demands to implement their plan as it is.

**Plan Integration**

City Municipal Council administration and function is limited to town level. Here plan integration of various departments is very necessary but it is not taking place. Because the administration unit and CB feel they are above all. This has resulted in an increase of drinking water problem and non-utilization of water treatment plant resources. With the co-ordination of TP this could be sorted out but owing to lack of co-ordination and increasing role of politics is required to solve urban and rural problems.
3-4. Rural and Urban Linkages in Planning and Budgeting

Integrated planning requires sectoral integration and spatial integration. Sectoral integration means the plans and budgets of different development sectors and the integration of different schemes pertaining to them. Spatial integration means the integration of the plans and budgets of rural and urban local bodies. According to the Constitution the integration of plans is vested with the DPC which is provisioned in the 74th Amendment that is with the purview of the urban planning. This seems to be a misfit so far as our study is concerned.

Our study clearly brings out that the rural plans and budgets and the urban plans and budgets are prepared entirely separately. The rural planning and budgeting is conducted by the three tier Panchayati Raj system where as the planning for urban local bodies is done by municipal councils and corporations. Rural local self-governments prepare their plans through the three tier system and send it to the state government; this is certainly the case so with statutory planning. The World Bank supported Grama Swaraj Planning and budgeting is an exception in the sense that the plans and budgets of GPs go directly to the state secretariat via the Taluk Panchayat skipping the Zila Panchayat. This of course is an exception.

The urban plans on the other hand are prepared by the municipal councils from Taluk level on ward and are sent directly to the office of the Deputy Commissioner in the district. The urban plans from the deputy commissioner’s office are then sent to the Directorate of Municipal Administration in the state capital that is Bangalore, in our case. The planning for urban bodies has no connection with rural planning. Both follow two different channels.

This is complicated by the fact that the DPC is dysfunctional in our study district. If the DPC is active it may integrate both the plans and send the combined plans and budgets to the state government. But this does not seem to be taking place.

We make a strong case for integration of rural and urban planning and budgeting from the Taluk level on wards; because often the Taluk towns represent the rural-urban continuum in the development process. The taluk-towns are semi-rural and semi-urban. Here is where most of the trading and commercial activity for the rural
citizen’s takes place. Most taluks have extensive grain markets and agricultural co-operatives situated in taluk towns. The Taluk Panchayat office is also physically located in the taluk town. Therefore the planning and budgeting should be combined for both rural and urban sectors from Taluk level onwards.

Another important factor is that the small towns that the taluk towns represent are badly neglected in terms of civic amenities. The planning of the taluk towns is a neglected area. This was apparent in our field work in all the taluks that we have visited. There is a contention in the literature on decentralisation that the urban planning itself is a neglected area. Given the rapid urbanization in the development process the taluks have nodal importance for development activity. Therefore the planning and budgeting of taluk and also district level urban planning should be provided sufficient attention.

In addition to the above there are strong fiscal reasons why the urban and rural planning and budgeting should be combined. The taluk and district towns have enormous potential for raising finances through taxation. The constitution at present provides for taxation powers only to Grama Panchayats. The other tiers and urban local bodies are exempt from this. This misses out large potential for local revenue augmentation. This is because as mentioned above the taluk and even district towns are the major hubs of commercial activity for rural as well as urban citizens. It is at these levels that trade, construction, and also service sectors such as health and education are concentrated. All these can be taxed for their services; plus their growth and development can be systematically planned.

The rural–urban linkages in planning and budgeting is important because at this level the so called urban areas are not entirely urban. They represent what is known in the development literature as ‘rur-urban’ representing a continuum between rural and urban areas. Finally, there is massive migration to these areas and that also makes compelling reason for combined planning and budgeting for rural and urban areas.
Chapter -4

Findings and Recommendations

Firstly, our study has shown that at the district level the District Planning Committee has been constituted in 2007-2008 but it has not held a single meeting so far and this leads us to the recommendation that DPCs should be activated immediately to take proper care of the budgeting and planning process at the district level.

Secondly, the study has shown that there are different kinds of plans operating at the district level and further down the local self-governments. For instance in Tumkur we have both statutory planning as well as the World Bank supported Grama Swaraj Planning. The modus operandi of the both is different. The district level officials and particularly taluk level officials have mentioned that the transparency and accountability of the ‘Grama Swaraj’ plan is better than the statutory planning. If this is the case so the lessons from the latter can be taken for statutory planning as well.

Thirdly, there is no sectoral integration of the plans prepared at all levels. This is true from the GP level to the District level. Planning and budgeting is done separately for each developmental scheme or programme. Combining of sectoral plans happens at the state level as the interviews with the state level officials show. But at both GP and TP level and at the municipal level the planning and budgeting is for different schemes and programmes.

Fourthly, the funds and functions are devolved to the local self-governments but sufficient numbers of functionaries are not devolved. Those who are devolved, particularly for TP and ZP levels, are on deputation from the various line departments. They are not trained in budgeting or planning.

Fifthly, this brings us to the capacity of local self-governments to plan. Our study shows that the best possible cases for planning and budgeting are to be seen for at the Gram Panchayat level and not at the higher levels. The GPs are attempting to plan and budget for their finances and functions but they need technical assistance.

Sixthly, the above mentioned technical assistance is possible only if there is adequate capacity building of the present staff in planning and budgeting or by
creation of a separate cadre for planning and budgeting at district and sub-district levels. Many of the officials interviewed mentioned this aspect.

Seventhly, it was also observed during the study that some institutions such as Watershed associations (known as ‘Sujala Scheme’ in Tumkur) are operating entirely separately from the Gram Panchayats. They have large amount of funds and should be brought under the PRIs. Some parallel bodies such as School Development and Monitoring Committee (SDMCs) have mixed experience. While they have interface with the GPs in some cases, in other cases they operate independently. This is a serious problem.

Eighthly, The Government of Karnataka has brought the SDMCs under the purview of the Gram Panchayats but that does not seem to be followed up in case of all Panchayats.

Ninthly, as one Planning Officer has perceptively noted, the local self-governments have a problem with the definition of development itself. Most of the planning and budgeting is done for civil construction works of small scale such as roads, buildings, drainage works or for compounds for different offices. The focus on social sector that is particularly on health and education directly is not there at the GP level. This needs to be stressed. Though it may be true that all levels of PRIs plan for drinking water and sanitation. This is only indirect focus on social sector. In a country where adult literacy is not cent percent there should be exclusive focus on schooling. And also on health; this is the case so at local level.

Tenthly, as we have noted in the report there is no spatial integration of plans at the present. Rural and urban local bodies should plan together to meet the increasing needs of urbanization and the specific physical situation of these urban bodies which represent a rural and urban continuum and not neat separation.

Eleventhly, we have observed in the field that inclusivity in the planning process is not fully inclusive. The marginalized sections such as STs and SCs and women members in them in particular are not sufficiently considered in the budgeting and planning process.

Lastly, while DPC is not functioning in this district, we have to look for good practices at the ground level that is at the Grama Panchayat level where the process is followed systematically with ward Sabha coming first, the Grama
Sabha planning next and the general body of the Panchayat is only finalizing
the plan prepared and approved by the Grama Sabha. This process can be
emulated elsewhere along with constitution and activation of DPCs.
Annexure -1

Plates
Annexure 2

Steps in the Plan Preparation
(As per the Expert Committee Report)

- Put together the available data for each local government
- Based on the data, prepare a Vision Document for 5 years (to identify the key reasons for backwardness/development shortcomings and address issues impeding development)
- To assist the DPC in preparing the Vision Document
- Based on the Vision Document/s the needs to be prioritized and goals set for 5 years.
- Draft plan preparation should start from Grama Sabha
- Grama Panchayat Plan
- Taluk Panchayat Plan (including GPs Plans)
- Zilla Panchayat Plan (including TPs Plans)
- Draft plan should be in accordance with the approved activity assignment, CSSs/CPSs and related programmes
- Draft plan should indicate the expected outcomes (production, employment, infrastructure and human development)

- **Draft plan and Resources**
  1. Own resources
  2. Transfers under SFC for development purpose
  3. Twelfth Finance Grants
  4. Untied grants for local planning
  5. CSSs/CPSs grants
  6. Grants for state plan schemes
  7. Grants under externally aided schemes

Community contributions

Annexure 3

Model Methodology of Plan Preparation
(As per RDPR and Planning Departments, GOK)

The GPs have to prepare a 5 to 10 year long-term plan and splitting it into annual plans based on local priorities. The four important elements that have to be considered while formulating the plan are:

1. Where are we? (Status/position with regard to social, economic and infrastructure development);

2. Where we have to reach? (Goals/targets to be achieved)
3. How we should reach? (Methodology, tools, strategies and technologies to be adopted)

4. How we should review the progress? (Monitoring the plan implementation)

To replicate the above at the TP, ZP and Urban Local Body level

**Annexure - 4**

**Functional Groups**
(For Vision Setting and Preparation and Integration of Plans)

**I - Health and Education Committee**

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<tbody>
<tr>
<td>1</td>
<td>President</td>
<td>President of Health and Education Standing Committee of ZP</td>
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<tr>
<td>2</td>
<td>Non-official Members</td>
<td>include knowledgeable members of Health and Education Standing Committee of ZP</td>
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<td>3</td>
<td>Members - Official</td>
<td>District Health and F W Officer</td>
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<td>DDPI</td>
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<tr>
<td></td>
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<td>District Adult Education Officer</td>
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<tr>
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<td>District Youth Services Officer</td>
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<tr>
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<td></td>
<td>Engineering Division Officer</td>
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<td>Outside Experts</td>
<td>Dr. N Sivanna and Dr. M. Devendra Babu, ISEC, Bangalore; Dr. Veerasekharappa, Associate Professor, Siddaganga Institute of Management, Tumkur.</td>
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<td>5</td>
<td>Member Secretary</td>
<td>Deputy Secretary (Adm), Z P.</td>
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<td>Subjects to be covered</td>
<td>Education, Health, Youth Services, Drinking water supply</td>
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</tbody>
</table>

Note: to focus more on the issues related to women and children
### II - Agriculture and Industries Committee

<table>
<thead>
<tr>
<th>1</th>
<th>President</th>
<th>President of Agriculture and Industries Standing Committee of Z P</th>
</tr>
</thead>
<tbody>
<tr>
<td>2</td>
<td>Non-official Members</td>
<td>include members of Agriculture and Industries Standing Committee</td>
</tr>
</tbody>
</table>
| 3  | Members - Official         | J D Agriculture  
                     DCF (Social Forestry)  
                     DD of AH and VS  
                     DD of Horticulture  
                     Sericulture  
                     Fisheries  
                     DIC |
| 4  | Outside Experts            | Dr. N Sivanna and Dr. M. Devendra Babu,; Dr. Veerasekharappa, ISEC, Bangalore.  
                     NGOs/ Experts/ Retired Officials (include local retired Agriculture and Industries Officers, NGO representative and other experts (leading industrialists) |
| 5  | Member Secretary           | Deputy Secretary (Dev), Z P |
| 6  | Subjects to be covered     | Agriculture, Horticulture, Sericulture, AH & VS, Fisheries, Forestry, Industry, etc. |

Note: To focus on non-farm and unorganised sectors

### III - Social Justice Committee

<table>
<thead>
<tr>
<th>1</th>
<th>President</th>
<th>President of Social Justice Standing Committee of Z P</th>
</tr>
</thead>
<tbody>
<tr>
<td>2</td>
<td>Non-official Members</td>
<td>include members of Social Justice Standing Committee</td>
</tr>
</tbody>
</table>
| 3  | Members - Official         | District Social Welfare Officer  
                     District Officer for BCM  
                     DD of Women and Child  
                     District Manager, SC/ST and BCM Corporations |
| 4  | Outside Experts            | Dr. N Sivanna and Dr. M. Devendra Babu,; Dr. Veerasekharappa, ISEC, Bangalore.  
                     NGOs/ Experts/ Retired Officials (include local retired officers of Social Welfare, Women and Child, Backward and Minorities Depts, NGO representative and other experts) |
| 5  | Member Secretary           | Project Director (DRDA) |
| 6  | Subjects to be covered     | Welfare of Women, Children, SCs/STs/BCs |

Note: Should be broad based and cross cutting - including nutrition, welfare of SCs and STs, marginalised groups, environment, backward areas, energy consumption etc.
### IV - Rural Development and Infrastructure Committee

<table>
<thead>
<tr>
<th></th>
<th>President</th>
<th>President of Finance, Audit and Planning Standing Committee of ZP</th>
</tr>
</thead>
<tbody>
<tr>
<td>2</td>
<td>Non-official Members</td>
<td>Project Director (DRDA)</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Chief Accounts Officer</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Chief Planning Officer</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Executive Engineers</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Selected Executive Officers of TPs</td>
</tr>
<tr>
<td>3</td>
<td>Members - Official</td>
<td>Dr. N Sivanna and Dr. M. Devendra Babu,; Dr. Veerasekharappa</td>
</tr>
<tr>
<td></td>
<td></td>
<td>ISEC, Bangalore,</td>
</tr>
<tr>
<td></td>
<td></td>
<td>NGOs/ Experts/ Retired Officials (include local retired Deputy</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Secretaries of ZP, Labour Dept, Engineers, NGO representative</td>
</tr>
<tr>
<td></td>
<td></td>
<td>and other experts)</td>
</tr>
<tr>
<td>4</td>
<td>Outside Experts</td>
<td>Deputy Secretary (Dev)</td>
</tr>
<tr>
<td>5</td>
<td>Member Secretary</td>
<td>Enable Secretary</td>
</tr>
<tr>
<td>6</td>
<td>Subjects to be covered</td>
<td>rural development, poverty alleviation, employment,</td>
</tr>
<tr>
<td></td>
<td></td>
<td>infrastructure etc.</td>
</tr>
</tbody>
</table>

### V - Resource Committee

<table>
<thead>
<tr>
<th></th>
<th>President</th>
<th>President of DPC</th>
</tr>
</thead>
<tbody>
<tr>
<td>2</td>
<td>Non-official Members</td>
<td>one Member from each Sectoral Committee</td>
</tr>
<tr>
<td>3</td>
<td>Members - Official</td>
<td>One Officer from each important sectoral Departments</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Dr. N Sivanna and Dr. M. Devendra Babu, ISEC, Bangalore; Dr.</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Veerasekharappa, Associate Professor, Siddaganga Institute of</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Management, Tumkur</td>
</tr>
<tr>
<td></td>
<td></td>
<td>NGOs/ Experts/ Retired Officials (include local retired Accounts</td>
</tr>
<tr>
<td></td>
<td></td>
<td>officers, Chartered Accountants NGO representative and other</td>
</tr>
<tr>
<td></td>
<td></td>
<td>experts)</td>
</tr>
<tr>
<td>5</td>
<td>Member Secretary</td>
<td>Chief Accounts Officer, Zilla Panchayat</td>
</tr>
<tr>
<td>6</td>
<td>Subjects to be covered</td>
<td>Programme based budgeting, Plan and non-plan grants, Tied and</td>
</tr>
<tr>
<td></td>
<td></td>
<td>untied grants, external aid etc.</td>
</tr>
</tbody>
</table>
### VI - Urban Development Committee

<table>
<thead>
<tr>
<th></th>
<th>President</th>
<th>Vice-President of DPC</th>
</tr>
</thead>
<tbody>
<tr>
<td>2</td>
<td>Non-official Members</td>
<td>Members representing Urban bodies in the DPC, Presidents of Standing Committees at the Urban body level.</td>
</tr>
<tr>
<td>3</td>
<td>Members - Official</td>
<td>Head of each civic functional divisions (Drinking water, roads, sanitation, housing, poverty, street lights etc.)</td>
</tr>
<tr>
<td>4</td>
<td>Outside Experts</td>
<td>Dr. N Sivanna and Dr. M Devendra Babu, ISEC, Bangalore; Dr. Veerasekharappa, Associate Professor, Siddaganga Institute of Management, Tumkur NGOs/ Experts/ Retired Officials (include local retired urban planners, Engineers (Electricity, Civil), Doctors, educationist, past presidents of ULB, local NGO representative and other experts)</td>
</tr>
<tr>
<td>5</td>
<td>Member Secretary</td>
<td>Project Director, Urban Cell</td>
</tr>
<tr>
<td>6</td>
<td>Subjects to be covered</td>
<td>All civic and infrastructure functions</td>
</tr>
</tbody>
</table>

Note: 1. To focus on rural urban linkage.  
2. Same Committee for each of the individual Urban Body (Taluk level)

### VII - Core Committee

<table>
<thead>
<tr>
<th></th>
<th>President</th>
<th>President of DPC</th>
</tr>
</thead>
<tbody>
<tr>
<td>2</td>
<td>Non-official Members</td>
<td>one member from each Standing Committee including Municipality)</td>
</tr>
<tr>
<td>3</td>
<td>Members - Official</td>
<td>One Officer from each important sectoral Departments</td>
</tr>
<tr>
<td>4</td>
<td>Outside Experts</td>
<td>Prof. R S Deshpande, Dr. N Sivanna and Dr. M. Devendra Babu, ISEC, Bangalore; Dr. Veerasekharappa, Associate Professor, Siddaganga Institute of Management, Tumkur NGOs/ Experts/ Retired Officials (include local retired Accounts officers, Chartered Accountants, NGO representative and other experts)</td>
</tr>
<tr>
<td>5</td>
<td>Member Secretary</td>
<td>CEO of ZP</td>
</tr>
<tr>
<td>6</td>
<td>Subjects to be covered</td>
<td>Vision setting, to integrate plans prepared by the Functional Committees at different levels</td>
</tr>
</tbody>
</table>
### Table 1

**Status of District Planning Committees in Major States, India**

<table>
<thead>
<tr>
<th>State</th>
<th>Status of DPC</th>
<th>Chairperson of DPC</th>
</tr>
</thead>
<tbody>
<tr>
<td>Andhra Pradesh</td>
<td>Not yet constituted</td>
<td>--</td>
</tr>
<tr>
<td>Assam</td>
<td>Not yet constituted</td>
<td>--</td>
</tr>
<tr>
<td>Bihar</td>
<td>Constituted</td>
<td>Chairperson of ZP</td>
</tr>
<tr>
<td>Chhatisgarh</td>
<td>Constituted</td>
<td>District In-Charge Minister</td>
</tr>
<tr>
<td>Gujarat</td>
<td>Not yet constituted</td>
<td>--</td>
</tr>
<tr>
<td>Haryana</td>
<td>Constituted</td>
<td>*</td>
</tr>
<tr>
<td>Karnataka</td>
<td>Constituted</td>
<td>Chairperson of ZP</td>
</tr>
<tr>
<td>Kerala</td>
<td>Constituted</td>
<td>Chairperson of DP</td>
</tr>
<tr>
<td>Madhya Pradesh</td>
<td>Constituted</td>
<td>District In-charge Minister</td>
</tr>
<tr>
<td>Jharkhand</td>
<td>Not yet constituted</td>
<td>--</td>
</tr>
<tr>
<td>Maharashtra</td>
<td>Not yet constituted</td>
<td>--</td>
</tr>
<tr>
<td>Orissa</td>
<td>Partially (in 26 districts)</td>
<td>District In-charge Minister</td>
</tr>
<tr>
<td>Punjab</td>
<td>Not yet constituted</td>
<td>--</td>
</tr>
<tr>
<td>Rajasthan</td>
<td>Constituted</td>
<td>Chairperson of ZP</td>
</tr>
<tr>
<td>Tamil Nadu</td>
<td>Constituted</td>
<td>Chairperson of ZP</td>
</tr>
<tr>
<td>Uttar Pradesh</td>
<td>Not yet constituted</td>
<td>--</td>
</tr>
<tr>
<td>Uttaranchal</td>
<td>Constituted</td>
<td>District In-charge Minister</td>
</tr>
<tr>
<td>West Bengal</td>
<td>Constituted</td>
<td>Chairperson of DP</td>
</tr>
</tbody>
</table>

**Note:** * Information not available

**Source:** Website of the Ministry of Panchayat Raj, Government of India.
<table>
<thead>
<tr>
<th>State</th>
<th>Number of Departments/Subjects Transferred to Panchayats with</th>
<th>Number of Departments /Subjects yet to be Transferred to Panchayats with</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Funds</td>
<td>Functions</td>
</tr>
<tr>
<td>Andhra Pradesh</td>
<td>5</td>
<td>17</td>
</tr>
<tr>
<td>Assam</td>
<td>0</td>
<td>29</td>
</tr>
<tr>
<td>Bihar</td>
<td>25</td>
<td>5</td>
</tr>
<tr>
<td>Jharkhand</td>
<td>^</td>
<td>^</td>
</tr>
<tr>
<td>Gujarat</td>
<td>15</td>
<td>15</td>
</tr>
<tr>
<td>Haryana</td>
<td>0</td>
<td>16</td>
</tr>
<tr>
<td>Karnataka</td>
<td>29</td>
<td>29</td>
</tr>
<tr>
<td>Kerala</td>
<td>26</td>
<td>26</td>
</tr>
<tr>
<td>Madhya Pradesh</td>
<td>10</td>
<td>23</td>
</tr>
<tr>
<td>Chhatisgarh</td>
<td>10</td>
<td>29</td>
</tr>
<tr>
<td>Maharashtra</td>
<td>18</td>
<td>18</td>
</tr>
<tr>
<td>Orissa</td>
<td>9</td>
<td>25</td>
</tr>
<tr>
<td>Punjab</td>
<td>0</td>
<td>7</td>
</tr>
<tr>
<td>Rajasthan</td>
<td>18</td>
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<td>29</td>
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<tr>
<td>Uttar Pradesh</td>
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<td>12</td>
</tr>
<tr>
<td>Uttarakanchal</td>
<td>0</td>
<td>11</td>
</tr>
<tr>
<td>West Bengal</td>
<td>12</td>
<td>29</td>
</tr>
</tbody>
</table>

**Note:** * - only functional control; ^ - Elections to PRIs have not yet been held

**Source:** Babu, 2007)
<table>
<thead>
<tr>
<th>State</th>
<th>1997-98 Own Revenue</th>
<th>1997-98 Transferred Revenue</th>
<th>1997-98 Total Revenue</th>
<th>2002-03 Own Revenue</th>
<th>2002-03 Transferred Revenue</th>
<th>2002-03 Total Revenue</th>
<th>% to row Totals</th>
<th>% to row Totals</th>
</tr>
</thead>
<tbody>
<tr>
<td>Andhra Pradesh</td>
<td>13779.69</td>
<td>237378.88</td>
<td>251158.57</td>
<td>17083.00</td>
<td>440830.00</td>
<td>457913.00</td>
<td>5.49</td>
<td>94.51</td>
</tr>
<tr>
<td>% to row Totals</td>
<td>5.49</td>
<td>94.51</td>
<td>100.00</td>
<td>3.73</td>
<td>96.27</td>
<td>100.00</td>
<td>5.49</td>
<td>94.51</td>
</tr>
<tr>
<td>Assam</td>
<td>345.99</td>
<td>1204.32</td>
<td>1550.31</td>
<td>761.00</td>
<td>0.00</td>
<td>761.00</td>
<td>22.32</td>
<td>77.68</td>
</tr>
<tr>
<td>% to row Totals</td>
<td>22.32</td>
<td>77.68</td>
<td>100.00</td>
<td>2.25</td>
<td>97.75</td>
<td>100.00</td>
<td>22.32</td>
<td>77.68</td>
</tr>
<tr>
<td>Bihar</td>
<td>0.00</td>
<td>36596.09</td>
<td>36596.09</td>
<td>667.00</td>
<td>28926.00</td>
<td>29593.00</td>
<td>0.00</td>
<td>100.00</td>
</tr>
<tr>
<td>% to row Totals</td>
<td>0.00</td>
<td>100.00</td>
<td>100.00</td>
<td>2.25</td>
<td>97.75</td>
<td>100.00</td>
<td>0.00</td>
<td>100.00</td>
</tr>
<tr>
<td>Gujarat</td>
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<td>323251.00</td>
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<td>98.19</td>
<td>100.00</td>
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<td>97.88</td>
<td>100.00</td>
<td>1.81</td>
<td>98.19</td>
</tr>
<tr>
<td>Haryana</td>
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<td>8522.00</td>
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<td>29801.00</td>
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</tr>
<tr>
<td>% to row Totals</td>
<td>62.20</td>
<td>37.80</td>
<td>100.00</td>
<td>20.82</td>
<td>79.18</td>
<td>100.00</td>
<td>62.20</td>
<td>37.80</td>
</tr>
<tr>
<td>Karnataka</td>
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<td>424357.00</td>
<td>430303.00</td>
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<td>97.75</td>
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<td>97.75</td>
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<td>73468.00</td>
<td>96069.00</td>
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<td>98.62</td>
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<tr>
<td>% to row Totals</td>
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<td>98.62</td>
<td>100.00</td>
<td>23.53</td>
<td>76.47</td>
<td>100.00</td>
<td>1.38</td>
<td>98.62</td>
</tr>
<tr>
<td>Madhya Pradesh</td>
<td>3203.83</td>
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<td>177901.47</td>
<td>17481.00</td>
<td>30370.00</td>
<td>47851.00</td>
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<td>98.20</td>
</tr>
<tr>
<td>% to row Totals</td>
<td>1.80</td>
<td>98.20</td>
<td>100.00</td>
<td>23.53</td>
<td>76.47</td>
<td>100.00</td>
<td>1.80</td>
<td>98.20</td>
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<td>486714.00</td>
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<tr>
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<td>96.61</td>
<td>100.00</td>
<td>8.81</td>
<td>91.19</td>
<td>100.00</td>
<td>3.39</td>
<td>96.61</td>
</tr>
<tr>
<td>Orissa</td>
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<td>18233.00</td>
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<td>98.91</td>
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<td>98.91</td>
<td>100.00</td>
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<td>97.07</td>
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<tr>
<td>Punjab</td>
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<td>97.07</td>
<td>100.00</td>
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</tr>
<tr>
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<td>177394.00</td>
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<td>2.02</td>
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<td>100.00</td>
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<td>97.92</td>
<td>100.00</td>
<td>2.02</td>
<td>97.98</td>
</tr>
<tr>
<td>Tamil Nadu</td>
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<td>42216.41</td>
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<td>82514.00</td>
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<td>% to row Totals</td>
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<td>97.92</td>
<td>100.00</td>
<td>2.08</td>
<td>97.92</td>
<td>100.00</td>
<td>2.08</td>
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</tr>
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<td>% to row Totals</td>
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<td>89.86</td>
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<td>94.72</td>
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<tr>
<td>West Bengal</td>
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<td>3127.00</td>
<td>14596.00</td>
<td>17723.00</td>
<td>3.50</td>
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</tr>
<tr>
<td>% to row Totals</td>
<td>3.50</td>
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<td>6.84</td>
<td>93.16</td>
<td>100.00</td>
<td>3.50</td>
<td>96.50</td>
</tr>
<tr>
<td>All States Total</td>
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<td>164351.00</td>
<td>2236701.00</td>
<td>2401052.00</td>
<td>3.50</td>
<td>96.50</td>
</tr>
<tr>
<td>% to row Totals</td>
<td>3.50</td>
<td>96.50</td>
<td>100.00</td>
<td>6.84</td>
<td>93.16</td>
<td>100.00</td>
<td>3.50</td>
<td>96.50</td>
</tr>
</tbody>
</table>

### Table 4

**Major Recommendations of First State Finance Commissions Of Major States in India**

<table>
<thead>
<tr>
<th>State</th>
<th>Recommendations</th>
<th>Status</th>
</tr>
</thead>
<tbody>
<tr>
<td>Andhra Pradesh</td>
<td>9.14% of the tax and non-tax revenue of the state PRIs</td>
<td>Accepted</td>
</tr>
<tr>
<td></td>
<td>Increase of per capita grant to GPs from Rs.1 to Rs.4, and to MPs Rs.5 to Rs.8,</td>
<td>Accepted</td>
</tr>
<tr>
<td></td>
<td>Rs.2 to Rs.4 for ZPs</td>
<td>Accepted</td>
</tr>
<tr>
<td>Bihar</td>
<td>SFC constituted</td>
<td>Details no available</td>
</tr>
<tr>
<td>Gujarat</td>
<td>SFC constituted</td>
<td>Details no available</td>
</tr>
<tr>
<td>Karnataka</td>
<td>Transferring 36% of state's non-loan gross revenue receipts</td>
<td>Accepted</td>
</tr>
<tr>
<td></td>
<td>85% to PRIs and 15% to Urban local bodies</td>
<td>Accepted</td>
</tr>
<tr>
<td>Kerala</td>
<td>25% of net motor vehicle tax collection to local bodies</td>
<td>Accepted</td>
</tr>
<tr>
<td></td>
<td>Proceeds of building tax to village panchayats and municipalities</td>
<td>Accepted</td>
</tr>
<tr>
<td></td>
<td>Earmarking a portion of the income from the sale of court fee stamps to LBs</td>
<td>Accepted</td>
</tr>
<tr>
<td>Madhya Pradesh</td>
<td>Grants to GPs to discharge their functions</td>
<td>Accepted</td>
</tr>
<tr>
<td></td>
<td>Agency fee to Janpad and ZPs for carrying out Agency functions</td>
<td>Accepted</td>
</tr>
<tr>
<td></td>
<td>For providing tied and untied grants</td>
<td>Not accepted</td>
</tr>
<tr>
<td></td>
<td>A lumpsum non-recurring grant</td>
<td>Accepted</td>
</tr>
<tr>
<td>Maharashtra</td>
<td>Total 129 recommendations (12 accepted)</td>
<td>Details not available</td>
</tr>
<tr>
<td></td>
<td>And records by each local body</td>
<td>Accepted</td>
</tr>
<tr>
<td></td>
<td>Share of state taxes for transfer to local bodies to be 2% in each year</td>
<td>Accepted</td>
</tr>
<tr>
<td></td>
<td>Transfer of 10% of net proceeds of MVT</td>
<td>Accepted</td>
</tr>
<tr>
<td>Orissa</td>
<td>Massive external assistance to local bodies to upgrade basic services</td>
<td>Not known</td>
</tr>
<tr>
<td></td>
<td>Surcharge on stamp duty for transfer of properties in rural areas</td>
<td>Not known</td>
</tr>
<tr>
<td>Punjab</td>
<td>Assignment of land revenue to GPs</td>
<td>Accepted</td>
</tr>
<tr>
<td></td>
<td>Sharing of 20% of the net proceeds of the stamp duties, MVT, electricity</td>
<td>Accepted</td>
</tr>
<tr>
<td></td>
<td>Duty and entertainment tax with PRIs and Municipalities</td>
<td>Accepted</td>
</tr>
<tr>
<td>Rajasthan</td>
<td>To devolve 2.18% of the net proceeds of the state's own tax revenue to PRIs</td>
<td>Accepted</td>
</tr>
<tr>
<td></td>
<td>To provide 50% matching grant</td>
<td>Accepted</td>
</tr>
<tr>
<td>Tamil Nadu</td>
<td>Assigning local cess surcharge on stamp duty to PRIs</td>
<td>Accepted</td>
</tr>
<tr>
<td></td>
<td>90% of entertainment tax to PRIs</td>
<td>Accepted</td>
</tr>
<tr>
<td></td>
<td>8% of total state tax revenues</td>
<td>Accepted</td>
</tr>
<tr>
<td>Uttar Pradesh</td>
<td>SFC constituted</td>
<td>Details not available</td>
</tr>
<tr>
<td>West Bengal</td>
<td>Sharing of 16% of the net proceeds of all taxes collected by state with PRIs and Municipalities</td>
<td>Accepted</td>
</tr>
</tbody>
</table>

### Table–5

Scheduled caste population of Tumkur

<table>
<thead>
<tr>
<th>S No</th>
<th>Taluk</th>
<th>Rural Total</th>
<th>Rural Male</th>
<th>Rural Female</th>
<th>Urban Total</th>
<th>Urban Male</th>
<th>Urban Female</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Tumkur</td>
<td>55414</td>
<td>28276</td>
<td>27138</td>
<td>29155</td>
<td>15260</td>
<td>13895</td>
</tr>
<tr>
<td>2</td>
<td>Kunegal</td>
<td>27436</td>
<td>13380</td>
<td>14056</td>
<td>3227</td>
<td>1635</td>
<td>1592</td>
</tr>
<tr>
<td>3</td>
<td>Thiptur</td>
<td>25406</td>
<td>12620</td>
<td>12786</td>
<td>5078</td>
<td>2596</td>
<td>2482</td>
</tr>
<tr>
<td>4</td>
<td>Gubbi</td>
<td>38780</td>
<td>19659</td>
<td>19121</td>
<td>2122</td>
<td>1068</td>
<td>1054</td>
</tr>
</tbody>
</table>

Source: Tumkur district at a glance 2005-06, Government of Karnataka

### Table–6

Scheduled tribe population of Tumkur

<table>
<thead>
<tr>
<th>S No</th>
<th>Taluk</th>
<th>Rural Total</th>
<th>Rural Male</th>
<th>Rural Female</th>
<th>Urban Total</th>
<th>Urban Male</th>
<th>Urban Female</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Tumkur</td>
<td>19641</td>
<td>10116</td>
<td>9525</td>
<td>9512</td>
<td>4944</td>
<td>4568</td>
</tr>
<tr>
<td>2</td>
<td>Kunegal</td>
<td>2231</td>
<td>1143</td>
<td>1088</td>
<td>223</td>
<td>111</td>
<td>112</td>
</tr>
<tr>
<td>3</td>
<td>Thiptur</td>
<td>6463</td>
<td>3275</td>
<td>3188</td>
<td>1347</td>
<td>693</td>
<td>654</td>
</tr>
<tr>
<td>4</td>
<td>Gubbi</td>
<td>17362</td>
<td>8786</td>
<td>8576</td>
<td>709</td>
<td>364</td>
<td>345</td>
</tr>
</tbody>
</table>

Source: Tumkur district at a glance 2005-06, Government of Karnataka
### Table – 7

**Literacy in Tumkur**

<table>
<thead>
<tr>
<th>S No</th>
<th>Taluk</th>
<th>Rural</th>
<th>Urban</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>Male</td>
<td>Female</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Total</td>
<td>Total</td>
<td>Male</td>
</tr>
<tr>
<td>1</td>
<td>Tumkur</td>
<td>157558</td>
<td>184544</td>
<td>342102</td>
</tr>
<tr>
<td></td>
<td></td>
<td>91466</td>
<td>100900</td>
<td>195166</td>
</tr>
<tr>
<td></td>
<td></td>
<td>63292</td>
<td>83644</td>
<td>146936</td>
</tr>
<tr>
<td>2</td>
<td>Gubbi</td>
<td>140606</td>
<td>12571</td>
<td>153177</td>
</tr>
<tr>
<td></td>
<td></td>
<td>81059</td>
<td>6820</td>
<td>87879</td>
</tr>
<tr>
<td></td>
<td></td>
<td>59547</td>
<td>5751</td>
<td>65298</td>
</tr>
<tr>
<td>3</td>
<td>Kunegal</td>
<td>106699</td>
<td>20660</td>
<td>127359</td>
</tr>
<tr>
<td></td>
<td></td>
<td>62274</td>
<td>11312</td>
<td>73586</td>
</tr>
<tr>
<td></td>
<td></td>
<td>44425</td>
<td>9348</td>
<td>53773</td>
</tr>
<tr>
<td>4</td>
<td>Thiptur</td>
<td>106015</td>
<td>39006</td>
<td>145021</td>
</tr>
<tr>
<td></td>
<td></td>
<td>60473</td>
<td>21226</td>
<td>81699</td>
</tr>
<tr>
<td></td>
<td></td>
<td>45542</td>
<td>17780</td>
<td>63322</td>
</tr>
</tbody>
</table>

Source: Tumkur district at a glance 2005-06, Government of Karnataka

### Table – 8

**Literacy rates in Tumkur district from 1951 to 2001**

(In Percentages)

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Tumkur</td>
<td>24.14</td>
<td>29.34</td>
<td>37.49</td>
<td>44.93</td>
<td>64.03</td>
<td>75</td>
</tr>
<tr>
<td>2</td>
<td>Gubbi</td>
<td>16.64</td>
<td>20.68</td>
<td>27.84</td>
<td>35.69</td>
<td>51.97</td>
<td>67.5</td>
</tr>
<tr>
<td>3</td>
<td>Kunegal</td>
<td>12.65</td>
<td>18.14</td>
<td>24.09</td>
<td>31.03</td>
<td>49.05</td>
<td>61.3</td>
</tr>
<tr>
<td>4</td>
<td>Thiptur</td>
<td>23.4</td>
<td>29.25</td>
<td>38.12</td>
<td>47.45</td>
<td>65.31</td>
<td>75</td>
</tr>
</tbody>
</table>

Source: Tumkur district at a glance 2005-06, Government of Karnataka
## Table 9

**Literacy Rate 1991 Census (In percentage)**

<table>
<thead>
<tr>
<th>S No</th>
<th>Taluk</th>
<th>Rural</th>
<th></th>
<th>Urban</th>
<th></th>
<th>Total</th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>Male</td>
<td>Female</td>
<td>Total</td>
<td>Male</td>
<td>Female</td>
<td>Total</td>
<td>Male</td>
<td>Female</td>
<td>Total</td>
<td>Male</td>
<td>Female</td>
<td>Total</td>
</tr>
<tr>
<td>1</td>
<td>Tumkur</td>
<td>65.92</td>
<td>40.74</td>
<td>53.55</td>
<td>82.24</td>
<td>70.66</td>
<td>78.12</td>
<td>74.04</td>
<td>52.88</td>
<td>64.03</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2</td>
<td>Gubbi</td>
<td>62.25</td>
<td>38.28</td>
<td>50.44</td>
<td>81.91</td>
<td>68.72</td>
<td>75.58</td>
<td>63.48</td>
<td>40.09</td>
<td>51.97</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>3</td>
<td>Kunegal</td>
<td>59.9</td>
<td>32.97</td>
<td>46.29</td>
<td>81.17</td>
<td>66.38</td>
<td>73.94</td>
<td>62.08</td>
<td>36.2</td>
<td>49.05</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>4</td>
<td>Thiptur</td>
<td>73.88</td>
<td>49.94</td>
<td>62.05</td>
<td>85.55</td>
<td>74.11</td>
<td>79.99</td>
<td>76.03</td>
<td>54.27</td>
<td>65.31</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Source: Tumkur district at a glance 2005-06, Government of Karnataka
### Table-10

**Literacy rate 2001 (In percentage)**

<table>
<thead>
<tr>
<th>S No</th>
<th>Taluk</th>
<th>Rural</th>
<th>Urban</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>Male</td>
<td>Female</td>
<td>Total</td>
</tr>
<tr>
<td>1</td>
<td>Tumkur</td>
<td>76.8</td>
<td>55.8</td>
<td>66.7</td>
</tr>
<tr>
<td></td>
<td></td>
<td>88.1</td>
<td>79.1</td>
<td>83.8</td>
</tr>
<tr>
<td></td>
<td></td>
<td>85.3</td>
<td>67.1</td>
<td>75</td>
</tr>
<tr>
<td>2</td>
<td>Gubbi</td>
<td>75.8</td>
<td>56.7</td>
<td>66.4</td>
</tr>
<tr>
<td></td>
<td></td>
<td>89.2</td>
<td>79.4</td>
<td>84.1</td>
</tr>
<tr>
<td></td>
<td></td>
<td>76.7</td>
<td>58.2</td>
<td>67.5</td>
</tr>
<tr>
<td>3</td>
<td>Kunegal</td>
<td>70.1</td>
<td>48</td>
<td>58.8</td>
</tr>
<tr>
<td></td>
<td></td>
<td>84.3</td>
<td>72.5</td>
<td>78.6</td>
</tr>
<tr>
<td></td>
<td></td>
<td>72</td>
<td>51</td>
<td>61.3</td>
</tr>
<tr>
<td>4</td>
<td>Thiptur</td>
<td>82.4</td>
<td>62.5</td>
<td>72.5</td>
</tr>
<tr>
<td></td>
<td></td>
<td>87.8</td>
<td>77.7</td>
<td>82.9</td>
</tr>
<tr>
<td></td>
<td></td>
<td>83.7</td>
<td>66.2</td>
<td>75</td>
</tr>
</tbody>
</table>

Source: Tumkur district at a glance 2005-06, Government of Karnataka

### Table-11

**Classification of workers**

<table>
<thead>
<tr>
<th>S No</th>
<th>Taluk</th>
<th>Other service</th>
<th>Total workers</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>Male</td>
<td>Female</td>
</tr>
<tr>
<td>1</td>
<td>Tumkur</td>
<td>87756</td>
<td>21011</td>
</tr>
<tr>
<td>2</td>
<td>Gubbi</td>
<td>15350</td>
<td>4100</td>
</tr>
<tr>
<td>3</td>
<td>Kunegal</td>
<td>17985</td>
<td>5296</td>
</tr>
<tr>
<td>4</td>
<td>Thiptur</td>
<td>28936</td>
<td>10188</td>
</tr>
</tbody>
</table>

Source: Tumkur district at a glance 2005-06, Government of Karnataka
**Table-12**

Rain fall patterns in Tumkur 2005 (In Mms)

<table>
<thead>
<tr>
<th>S No</th>
<th>Taluk</th>
<th>Working</th>
<th>Not working</th>
<th>Rain gauge</th>
<th>Normal rain fall</th>
<th>Actual Rain fall</th>
<th>Rainy days</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Tumkur</td>
<td>7</td>
<td>Not working</td>
<td>937.5</td>
<td>586.1</td>
<td>60</td>
<td></td>
</tr>
<tr>
<td>2</td>
<td>Gubbi</td>
<td>7</td>
<td>-</td>
<td>626.6</td>
<td>572.4</td>
<td>39</td>
<td></td>
</tr>
<tr>
<td>3</td>
<td>Kunegal</td>
<td>8</td>
<td>1</td>
<td>1139.8</td>
<td>680</td>
<td>58</td>
<td></td>
</tr>
<tr>
<td>4</td>
<td>Thiptur</td>
<td>5</td>
<td>-</td>
<td>827.1</td>
<td>503</td>
<td>39</td>
<td></td>
</tr>
</tbody>
</table>

Source: Tumkur district at a glance 2005-06, Government of Karnataka

**Table-13**

Taluk wise Literacy Rates as per 2001 census

(In percentage)

<table>
<thead>
<tr>
<th>Year</th>
<th>Taluk</th>
<th>2001</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>C N Halli</td>
<td>70.2</td>
</tr>
<tr>
<td>2</td>
<td>Gubbi</td>
<td>67.5</td>
</tr>
<tr>
<td>3</td>
<td>Koratagere</td>
<td>62.7</td>
</tr>
<tr>
<td>4</td>
<td>Kunegal</td>
<td>61.3</td>
</tr>
<tr>
<td>5</td>
<td>Madhugiri</td>
<td>61.2</td>
</tr>
<tr>
<td>6</td>
<td>Pavagada</td>
<td>56.5</td>
</tr>
<tr>
<td>7</td>
<td>Sira</td>
<td>62.4</td>
</tr>
<tr>
<td>8</td>
<td>Thiptur</td>
<td>75</td>
</tr>
<tr>
<td>9</td>
<td>Tumkur</td>
<td>75</td>
</tr>
<tr>
<td>10</td>
<td>Turuvekere</td>
<td>71.4</td>
</tr>
</tbody>
</table>

Source: - Tumkur district at a glance
Table-14

Taluk wise Sex Ratio of Tumkur District as per 2001 Census
(In percentage, Number Female for 1000 Male)

<table>
<thead>
<tr>
<th>Year</th>
<th>Taluk</th>
<th>2001</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>C N Halli</td>
<td>985</td>
</tr>
<tr>
<td>2</td>
<td>Gubbi</td>
<td>976</td>
</tr>
<tr>
<td>3</td>
<td>Koratagere</td>
<td>965</td>
</tr>
<tr>
<td>4</td>
<td>Kunegal</td>
<td>1023</td>
</tr>
<tr>
<td>5</td>
<td>Madhugiri</td>
<td>962</td>
</tr>
<tr>
<td>6</td>
<td>Pavagada</td>
<td>955</td>
</tr>
<tr>
<td>7</td>
<td>Sira</td>
<td>960</td>
</tr>
<tr>
<td>8</td>
<td>Thiptur</td>
<td>978</td>
</tr>
<tr>
<td>9</td>
<td>Tumkur</td>
<td>924</td>
</tr>
<tr>
<td>10</td>
<td>Turuvekere</td>
<td>1000</td>
</tr>
</tbody>
</table>

Source: - Tumkur district at a glance

Table-15

Details of Health institutions as on 31-3-2006

<table>
<thead>
<tr>
<th>S No</th>
<th>Taluks</th>
<th>Community Health Centre</th>
<th>Dispensaries</th>
<th>Family Welfare</th>
<th>Sterilization</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>Number</td>
<td>Beds</td>
<td>Allopathy</td>
<td>Indian System of Medicine</td>
</tr>
<tr>
<td>1</td>
<td>C N Halli</td>
<td>1</td>
<td>0</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>2</td>
<td>Gubbi</td>
<td>1</td>
<td>0</td>
<td>0</td>
<td>1</td>
</tr>
<tr>
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<td>0</td>
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</tr>
<tr>
<td>5</td>
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<td>0</td>
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</tr>
<tr>
<td>6</td>
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</tr>
<tr>
<td>7</td>
<td>Sira</td>
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<td>0</td>
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</tr>
<tr>
<td>8</td>
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<tr>
<td>9</td>
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</tr>
<tr>
<td>10</td>
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<td>0</td>
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<td>7</td>
<td>0</td>
<td>1</td>
<td>4</td>
</tr>
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Source: - Tumkur district at a glance
### Table-16

**Details of Health institutions in Tumkur as on 31-3-2006**

<table>
<thead>
<tr>
<th>S No</th>
<th>Taluks</th>
<th>Allopathy Hospitals</th>
<th>Indian System of Medicine Hospital</th>
<th>Private Hospitals (including Nursing Homes)</th>
<th>Primary Health Centers Health units</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>Number</td>
<td>Beds</td>
<td>Number</td>
<td>Beds</td>
</tr>
<tr>
<td>1</td>
<td>C N Halli</td>
<td>0</td>
<td>0</td>
<td>2</td>
<td>6</td>
</tr>
<tr>
<td>2</td>
<td>Gubbi</td>
<td>0</td>
<td>0</td>
<td>5</td>
<td>5</td>
</tr>
<tr>
<td>3</td>
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<td>30</td>
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<td>1</td>
<td>50</td>
<td>4</td>
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<tr>
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<td>0</td>
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</tr>
<tr>
<td>7</td>
<td>Sira</td>
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<td>0</td>
<td>3</td>
<td>0</td>
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<tr>
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<tr>
<td>9</td>
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<tr>
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<td>4</td>
<td>455</td>
<td>30</td>
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Source: - Tumkur district at a glance

### Table-17

**Details of High Schools in Tumkur as on 31-3-2006**

<table>
<thead>
<tr>
<th>Taluks</th>
<th>Government</th>
<th>Aided</th>
<th>Un aided</th>
<th>Total</th>
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<tbody>
<tr>
<td></td>
<td>Schools</td>
<td>Boys</td>
<td>Girls</td>
<td>Schools</td>
</tr>
<tr>
<td>C N Halli</td>
<td>13</td>
<td>1801</td>
<td>1745</td>
<td>29</td>
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<tr>
<td>Gubbi</td>
<td>20</td>
<td>2758</td>
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<td>25</td>
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<td>Koratagere</td>
<td>12</td>
<td>2363</td>
<td>2232</td>
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<td>Kunegal</td>
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<td>4029</td>
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<tr>
<td>Pavagada</td>
<td>11</td>
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<td>Sira</td>
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<td>3422</td>
<td>3397</td>
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<tr>
<td>Thiptur</td>
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<td>2193</td>
<td>25</td>
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<tr>
<td>Tumkur</td>
<td>17</td>
<td>2727</td>
<td>3701</td>
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### Details of Higher primary schools as on 31-3-2006

<table>
<thead>
<tr>
<th>S No</th>
<th>Taluks</th>
<th>Government</th>
<th>Aided</th>
<th>Un aided</th>
<th>Total</th>
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</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>Boys</td>
<td>Girls</td>
<td>Boys</td>
<td>Girls</td>
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<td>C N Halli</td>
<td>112</td>
<td>2985</td>
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<td>4168</td>
<td>3841</td>
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<td>40877</td>
<td>40421</td>
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Source: - Tumkur district at a glance

### Details of High school, Primary school, higher primary school and Pre-university

<table>
<thead>
<tr>
<th>S No</th>
<th>Taluks</th>
<th>Primary schools and Higher primary schools</th>
<th>High schools</th>
<th>Pre-University</th>
</tr>
</thead>
<tbody>
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<td></td>
<td></td>
<td>Schools Boys Girls</td>
<td>Schools Boys Girls</td>
<td>Schools Boys Girls</td>
</tr>
<tr>
<td>1</td>
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<td>355 13037 12236</td>
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<td>10 1050 1221</td>
</tr>
<tr>
<td>2</td>
<td>Gubbi</td>
<td>431 16032 15154</td>
<td>60 6777 7096</td>
<td>17 1486 1630</td>
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<tr>
<td>3</td>
<td>Koratagere</td>
<td>254 10268 9790</td>
<td>30 4325 3794</td>
<td>8 2223 1009</td>
</tr>
<tr>
<td>4</td>
<td>Kunegal</td>
<td>458 15131 14699</td>
<td>57 6535 6112</td>
<td>13 1145 1381</td>
</tr>
<tr>
<td>5</td>
<td>Madhugiri</td>
<td>381 18003 17037</td>
<td>56 8732 7836</td>
<td>16 1624 1332</td>
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<tr>
<td>6</td>
<td>Pavagada</td>
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<td>49 6021 4942</td>
<td>12 1918 1285</td>
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<td>7</td>
<td>Sira</td>
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<td>64 7672 6297</td>
<td>15 1249 1254</td>
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<td>634 35577 31442</td>
<td>125 17555 14621</td>
<td>49 6851 5919</td>
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<tr>
<td>10</td>
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<td>340 10114 9693</td>
<td>50 3948 3755</td>
<td>11 1038 1262</td>
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<td>3871 171089 160655</td>
<td>588 71167 63833</td>
<td>167 20559 18363</td>
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Source: - Tumkur district at a glance
**Table - 20**

**Normal and Average Rainfall of Tumkur District for the Year 2005 (In Mms)**

<table>
<thead>
<tr>
<th>Months</th>
<th>Normal rain</th>
<th>Actual Average Rain</th>
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<td>8.7</td>
</tr>
<tr>
<td>Feb</td>
<td>2.2</td>
<td>7.7</td>
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<tr>
<td>Mar</td>
<td>3.5</td>
<td>1.8</td>
</tr>
<tr>
<td>Apr</td>
<td>26.1</td>
<td>55</td>
</tr>
<tr>
<td>May</td>
<td>70.4</td>
<td>68.5</td>
</tr>
<tr>
<td>Jun</td>
<td>42.9</td>
<td>40.8</td>
</tr>
<tr>
<td>Jul</td>
<td>50.7</td>
<td>148.7</td>
</tr>
<tr>
<td>Aug</td>
<td>57.8</td>
<td>119.4</td>
</tr>
<tr>
<td>Sep</td>
<td>111.4</td>
<td>82.4</td>
</tr>
<tr>
<td>Oct</td>
<td>131.2</td>
<td>240.6</td>
</tr>
<tr>
<td>Nov</td>
<td>35.7</td>
<td>57.8</td>
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<tr>
<td>Dec</td>
<td>7.9</td>
<td>2.9</td>
</tr>
</tbody>
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Source: - Tumkur district at a glance
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ISS: http://www.localgovernmentindia
Fiscal Relations between the Centre and the States: Dependence of States on Devolution of Funds
Acknowledgements

We are thankful to the Commission for the Centre State Relations for entrusting this study to us. We have benefited considerably from discussions with the late Dr. Amaresh Bagchi and Mr. Dhirendra Singh, Hon'ble Member of the Commission. It was initial discussions with them that gave rise to undertaking a study on the Reference asking the Commission to examine "the impact of the recommendations made by the Eighth to Twelfth Finance Commissions on the fiscal relations between the Centre and the States, especially the greater dependence of the States on devolution of funds from the Centre." At the MSE, we have benefited from our discussions with Dr. C. Rangarajan and Dr. R.J. Chelliah on the subject of Centre-State Financial relations. We are also thankful to Dr. K. R. Shanmugam who took the trouble of going through all the Chapters and made valuable suggestions.

In the preparation of the manuscript we have been helped considerably by Ms. Sudha and Ms. Jothi at Madras School of Economics.

We are thankful to all of them for their help at various stages in the completion of this study.

D. K. Srivastava
Bhujanga C. Rao
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<td>1-17</td>
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<td>19-39</td>
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on the Relative Scope of Articles 275 and 282 (Para 7.9)
Executive Summary

Scope

1. The Commission on Centre-State Relations has been asked as part of its Terms of Reference to examine “the impact of the recommendations made by the Eighth to Twelfth Finance Commissions on the fiscal relations between the Centre and the States, especially the greater dependence of the States on devolution of funds from the Centre”. This term of reference has two key components: (a) fiscal relations between the centre and the states with the dependence of states on devolution of fund from the centre as a key feature of these relations, and (b) the impact on these by the recommendations of the Finance Commissions.

2. Healthy and efficient fiscal relations require that the relative autonomy of the states in undertaking expenditures according to their preferences and understanding of needs of their citizens be maintained. Dependence of states on devolution of funds from the centre may be considered in both quantitative and qualitative terms. A stable pattern of dependence implies that there is no tendency towards overcentralisation either of revenues or expenditures.

3. In this study, the pattern of states’ dependence on central transfers are analyzed by examining the share of such transfers in states’ revenue receipts. This has been done for the states as a whole as well as for individual states. Transfers consist of states’ share in central taxes, grants recommended by the Finance Commission, and other grants.

Features of India’s Federal Fiscal Structure

4. India’s federal structure consists of a central government, twenty-eight states, two Union Territories with legislatures, five Union Territories without own legislatures, several autonomous regions within states. States are characterized by considerable heterogeneity affecting their fiscal capacity, needs and costs of providing public services.

5. A vertical imbalance has been in-built in the scheme of assignment of resources and responsibilities provided in the constitution. For raising revenues, there is a need to obtain economies of scale and efficiency which is facilitated by uniform laws and a harmonious tax rate structure throughout the country so as to provide an integrated countrywide market. States are given a larger share of responsibilities because they understand the local needs and conditions better, and can generally reflect better the preferences of the people living in their jurisdictions. The vertical imbalance should be resolved by transferring resources from the centre to the state governments in an objective
and transparent manner. In addition, there is a horizontal imbalance, which arises because some states, compared to others, have larger resources because of their higher level of development and natural endowments. It is often the case that states with larger needs have relatively less resources and the horizontal imbalance may be quite large. The horizontal imbalance can be resolved by transferring relatively more to those states that have less resources and larger needs, so that certain minimum standards of certain important public and merit services can be ensured to all citizens. This equity objective should not lead to a methodology of transfers that gives rise to adverse incentives such that states begin to unduly depend on the central transfers rather than fully exploit their own resource bases. The system of fiscal transfers in a federal system must resolve both the vertical and horizontal imbalances in a fair and equitable manner that does not compromise the efficiency of the system.

6. The institution of the Finance Commission has been provided in the Constitution to resolve both vertical and horizontal imbalances. But transfers of funds from the centre to the states in India take place through three channels: Finance Commission, Planning Commission, and through various Central Ministries. This segmentation of transfers, particularly when the forms of transfers other than those provided by the Finance Commission become large and be determined in ad hoc and discretionary manner. These segments of transfers also have important inter-linkages and affect fiscal relations between the centre and the states in significant ways.

Sharing of Central Taxes

7. The Finance Commission recommends devolution of funds to the states under two modes of transfers: (a) share in central taxes and (b) grants under Article 275 of the Constitution. The approach of the Finance Commissions in both cases has evolved over time taking into consideration some important constitutional amendments.

8. Two important constitutional amendments during the period covered by the Eighth to the Twelfth Finance Commission are the 80th and 88th Amendments to the Constitution. The 80th Amendment relates to the alternative scheme of devolution recommended by the Tenth Finance Commission. Although the central government had accepted to implement the alternative scheme with effect from the beginning of the award period of the Tenth Finance Commission, the actual amendment was carried out only in 2000.

9. The 80th Amendment brought all central taxes, excluding Article 268 and 269 taxes and earmarked cesses and surcharges, under Article 270 for sharing with the states under the recommendations of the Finance Commissions. The 88th Amendment however placed
the service tax outside of this generalized arrangement of sharing. In addition, the central
government also began to rely relatively more on cesses and surcharges.

10. With the comprehensive sharing arrangement, under the provision of the amended
Article 270, the Finance Commissions have been able to develop a common set of criteria
for all central taxes and follow an approach to the devolution of funds consistent with
some of the agreed principles of fiscal transfers in the literature. However, subsequent to
the 80th Amendment, the central government has attempted to create additional fiscal
space for itself by relying relatively more on cesses and surcharges, and by placing the
service tax under Article 268. Both of these are the exceptions to the provision of globalised
sharing under Article 270.

Determination of Grants

11. In relation to grants there has been a debate regarding the scope of Articles 275 and
282, and the links between grants given by the Finance Commission and the assistance
given by the Planning Commission to the states. In the case of grants the approach of the
Finance Commission is constrained by the way the terms of reference are cast by the
central government. In particular, there is a reference to levels of tax and non-tax revenues
reached in a base year. An elaborate set of terms of reference is prepared with mandatory
clauses like the Commission ‘shall’ use a variety of considerations. There is also an
asymmetry between the way in which needs of the central government are referred to vis-
à-vis those of the states.

12. Various Finance Commissions themselves have followed an approach to determining
grants-in-aid, which contains adverse incentives as the approach is partially normative
and partially based on historical trends. This is not consistent with the first principles in
the determination of grants as considered acceptable in the literature on the subject. This
is also not consistent with the principles enunciated by the First Finance Commission
itself. The problem is aggravated because of the dynamic linkages between the Finance
Commission grants and plan assistance. Plan assistance is based partially on borrowing by
the states. This gives rise to committed expenditures in the form of interest payments,
salary and pension liabilities. Since, a large part of plan assistance has been used for
additional employment in the states giving rise to salary and pension liabilities. The Finance
Commissions generally take these committed expenditures as given or as historically
determined, thereby providing an incentive for the states to generate additional committed
liabilities independent of its fiscal capacity or own revenue effort based on borrowing.
Growing committed expenditures as a result of the mechanism of plan assistance also
imply growing dependence.
Dependence of States on Devolution of Funds

13. We have studied the pattern of dependence of the states on devolution of funds from the centre over the period covered by recommendations of the Eighth to the Twelfth Finance Commissions for which data are available i.e., from 1984-85 to the budget estimates of 2007-08 (RE). Prior to this, we look at the relative share of the centre and states in their combined revenue receipts. We find that the share of the states in the combined revenue receipts of the centre and the state governments net of intergovernmental flows, prior to transfers, shows that there has been an increase in the share of states from 35 per cent during 1984-89 to 39 per cent during 2001-05. After that it has fallen by about 2 percentage points.

14. The share of states in the combined revenue receipts after transfers shows that the relative availability of funds gets reversed as compared to the picture before transfers. In particular, the share of the centre, which was more than 60 per cent of the combined revenue receipts before transfers declines to about 35-38 per cent after transfers. In general, there is relative stability in the share of the centre and the states in the combined revenue receipts after transfers.

15. Considering dependence of the states on central taxes, which is measured by the ratio of states’ share in central taxes as percentage of states revenue receipts, the average for the period covered by respective Finance Commissions from the Eighth Commission onwards indicates that this ratio was about 22 per cent or just above for Eighth, Ninth, Eleventh and Twelfth Finance Commission periods. In the case of Tenth Commission, it was about 23.5 per cent. The share of states in central taxes as percentage of gross central revenues has also been stable in the range of 25-27 per cent. This share however is still less than the benchmark of 29 per cent, which was recommended by the Tenth Finance Commission while outlining the alternative scheme of devolution.

16. The dependence of state on devolution of funds from the centre is looked at in terms of the share of total transfers (share in taxes plus all grants) as percentage of states revenue receipts also indicates a pattern of stability. During the period covered by the Eighth to Twelfth Finance Commission, this ratio has varied in the range of 38-43 per cent.

17. Considering individual states, the pattern of dependence indicates that apart from a very limited number of states such as Bihar and to some extent West Bengal, there is no evidence of increased dependence of the states on devolution of funds from the centre.

18. The composition of transfers between states’ share in central taxes and grants (covering both Finance Commission grants and other grants) indicates a pattern, which is
by and large stable. States’ share in central taxes has been on average about 56 per cent of total transfers with some variations and correspondingly the share of grants has been about 44 per cent.

19. Fiscal relations between the centre and the states are affected more by qualitative dimensions of fiscal relations rather than quantitative dimensions. In particular, the following aspects are notable:

The central government has relied to a considerable extent on additional cesses and surcharges, particularly in recent years. Even though part of the cesses may be allocated to the states, such allocation mechanisms tend to be non-transparent and discretionary.

Even in the case of plan grants there is less reliance on the Gadgil formula and a larger portion of it is being allocated in an ad hoc manner.

(a) Placement of service tax under Article 268A rather than under Article 270 is also not conducive to maintenance of healthy fiscal relations between the centre and the states, even though at present the same share of service tax is being given to the states as for other central taxes.

(b) The approach of the Finance Commission is also affected by the way the terms of reference are cast. In particular, Finance Commission is mandated to use some specific year as ‘base’ year. In addition, they have to provide for considerable liabilities due to the mechanism of plan assistance, which has a limited time perspective, and does not provide for the implications of the long-term liabilities created by the plan process on state finances.

(c) The Finance Commissions have not been able to resolve the horizontal imbalance among states, and there is evidence of growing inequalities, which is not healthy for fiscal relations between the centre and the states.

(d) The central government unilaterally decides about issues relating expenditures and revenues that have vertical externalities.

(e) Many of the ‘non-financial’ recommendations of the Finance Commissions relating to a permanent secretariat, synchronization of periods of five year plans and Finance Commission recommendation periods, centrally sponsored schemes, financial autonomy for Finance Commission have also not been given due attention by the central government. These would help in establishing a better institutional framework for managing healthy fiscal relations between the centre and the states.
Transfers of Funds to States:  
The Constitutional Scheme

1.1 Introduction

The Commission on Centre-State Relations has been asked as part of its Terms of Reference to examine "the impact of the recommendations made by the Eighth to Twelfth Finance Commissions on the fiscal relations between the Centre and the States, especially the greater dependence of the States on devolution of funds from the Centre."

The scope of the term 'fiscal relations' between the centre and the states needs to be understood in context of a healthy and efficient working of the fiscal federal system. Healthy and efficient fiscal relations require that the relative autonomy in undertaking expenditures by the state governments according to their preferences and their understanding of needs of their citizen is maintained. Fiscal relations would not be considered healthy or efficient if there is excessive centralization of expenditures or revenue. There would be over centralization of expenditures if the central government insists on spending on heads that belong to the State List or by overly occupying the heads under the Concurrent List. One aspect of over centralization is for the centre to by pass the states and transfer funds directly to local bodies.

The dependence of the states, for financing their expenditures on devolution of funds from the centre, is one aspect of these relations. Dependence of states on central transfers can be studied through the share of central transfers in a state's revenue receipts or revenue expenditures. Since part of the revenue expenditures can be financed by borrowing, in this study, we study the pattern of states' dependence on central transfers by examining the share of such transfers in states' revenue receipts. This has been done for the states as a whole and for individual states. However, even if this dependence may not have altered for states as a group, the quality of fiscal relations may be affected if the autonomy of the states in deciding their expenditure
priorities is largely or partially affected by the way transfers of resources are made from the centre to the states. Since these transfers come not only from the Finance Commissions but also through the plan transfers and through various centrally sponsored schemes, there may be undue conditionalities attached to such transfers and there may also be greater adhocism and non-transparency exercised by the central government in the process of allocation of funds to the states. Fiscal relations are also vitiated if the central government usurps, for itself, sources of revenue taking advantage of its residual powers. These features may be hidden even behind a stable dependency ratio. Furthermore, even if the Finance Commission devolution may be transparent and largely based on principles and formulae, there is a dynamic linkage between Finance Commission transfers and other channels of transfers. This arises because of committed expenditures that get generated as a result of additional recruitment for administering plan schemes and similar other central initiatives.

It is also worth examining, whether the deterioration of fiscal relations between the centre and the states is due to increased dependence of states on the centre or other qualitative aspects of fiscal relations, and how far the recommendations of the Finance Commissions may have had a bearing on this.

Some of these issues got discussed just about the time the recommendation period of the Eighth Finance commission was ending and that of the Ninth Finance Commission was about to begin. In February 1988, the Chief Ministers of seven opposition ruled states confronted the then Prime Minister, Shri Rajeev Gandhi, on the question of financial autonomy of states. Their mood describing summarily the state of non-consonance between the ruling party at the centre and those in a number of states, was summed up by Shri Hedge at a joint press conference held at New Delhi following this meeting with the Prime Minister in the following words: "The rulers in New Delhi seem to be forgetting that India is an Union" (The Pioneer, February 10, 1988). One of the foremost issues was, 'a very large degree of over-centralization, reducing the states to mere administrative agencies of the Union'. It was alleged that the Union has managed to occupy most of the concurrent field leaving little for the states by indiscriminately making declarations of public interest or national importance taking over excessive areas of the linked entries in the state field.

Later in the year, in a meeting of the National Development Council at New Delhi, which was marked by sharp exchanges between the then Prime Minister and some of the Chief Ministers, Shri Hedge made a number of succinct remarks. He observed:
"The web of relationship as worked into our constitution is so complex that the only atmosphere in which the centre and the states must work is one of co-operation and not competition. The greatest threat to co-operative effort is betrayal of trust and self-aggrandizement by one of the parties (the Government of India) …. We must establish the norms of consultation clearly. The Government of India not only seems to regard consultations with the states beneath its dignity, but seems to revel in riding roughshod over their rights and interests." (The Pioneer, July 8, 1988)

Fiscal relations have been vitiated because fiscal transfers have not been able to reduce inequalities across states. Observe for example, some comments: "The upshot of these assertions by huge states like Uttar Pradesh, Bihar and Orissa, who had kept quiet for many years seems to indicated the highly tension ridden state of Union-state financial relations in the wake of continued growth of inter-regional disparities, complete breakdown of intra-party mechanism of resolving such issues and a perceptible increase in regional passions." (Sathyamurthy, 1989, p. 2134)

In this Chapter, we examine the basic constitutional arrangements governing the relations between the centre and the states, the duties and responsibilities of the Finance Commission, and the alternative sources of devolution of funds from the centre to the states.

In Chapter 2, we examine the main changes brought about by the Finance Commissions affecting devolution of funds from the centre to the states, during the periods of awards covered by the Eighth to Twelfth Finance Commissions.

In Chapter 3, we examine the pattern of dependence of states on transfers of funds from the centre during the period 1984-85 to 2008-09 covering the period of award of the Eighth to Twelfth Commissions. We also examine the qualitative aspects of management of fiscal transfers to the states.

Chapter 4 provides the concluding observations regarding the issues of transfer of funds from the centre to the states with a view to making these more stable as well as determined by first principles rather than ad hoc considerations. It also indicates measures to improve the fiscal relations between the centre and the states.

1.2 Features of India's Federal Fiscal Structure

India's federal structure consists of a central government, twenty-eight states, two
Union Territories with legislatures, five Union Territories without own legislatures, several autonomous regions within states. The three most recently created states are those of Uttarakhand (now known as Uttarakhand), Chhattisgarh, and Jharkhand. There is also a three-tier structure of rural local bodies and three levels of urban local bodies. As per the nomenclature used by the Planning Commission, eleven states are categorized as special category states. Critical institutions that intermediate between the central, state and local governments are the Finance Commission, the Planning Commission, the Inter-State Council, the National Development Council (NDC), and State Finance Commissions (SFCs), one for each state. While the Planning Commission is a permanent body, the central and state level Finance Commissions are set up with a normal periodicity of five years.

There is considerable heterogeneity among states in terms of their size and other features. Uttar Pradesh, even after the creation of Uttarakhand in 2000, is still the state with the largest population. Sikkim is the state with the smallest population size. In terms of population, as per 2001 census data, Uttar Pradesh is nearly 332 times as large as Sikkim. The state with the lowest per capita Gross State Domestic Product (GSDP) is Bihar, and the highest per capita Gross State Domestic Product is that for Goa, the ratio of the richest to the poorest being 8.7 for 2006-07 considering these at current prices (Table 1.1). At constant prices (1999-00), this ratio is 6.9. Since Goa is a small state, it can be excluded for this kind of comparison. Excluding Goa, the ratio of the highest to lowest per capita GSDP at current and constant prices respectively for 2006-07 are 5.2 and 4.7. States that may be listed as the five highest income states, considering per capita Gross State Domestic Product as an indicator of per capita income are Goa, Haryana, Punjab, Maharashtra, and Gujarat among the non-special category states.

In terms of area, the largest state is Rajasthan followed by Madhya Pradesh, Maharashtra and Uttar Pradesh. The smallest state in terms of area is Goa, followed by Sikkim and Tripura. Many of the special category states have small areas, but Jammu and Kashmir, and Assam have relatively larger areas, and Himachal Pradesh and Uttarakhand are middle sized states in terms of area. The area of Rajasthan is nearly 92.5 times that of Goa (Table 1.1). Thus, the Indian federal structure is characterized by considerable heterogeneity in terms of size of population, area and per capita income. These effect fiscal capacities of the states and also lead to differences in cost in the provision of publically provided services. Differences in fiscal capacities translate into differences in
## Table 1.1
**States in India: Comparison of Selected Parameters**

<table>
<thead>
<tr>
<th>State</th>
<th>Area of States ('000 sq. km)</th>
<th>Population 2001 (Crore)</th>
<th>Per Capita GSDP 2006-07 (Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Andhra Pradesh</td>
<td>275.05</td>
<td>7.62</td>
<td>33,142</td>
</tr>
<tr>
<td>Arunachal Pradesh</td>
<td>83.74</td>
<td>0.11</td>
<td>27,876</td>
</tr>
<tr>
<td>Assam</td>
<td>78.44</td>
<td>2.67</td>
<td>22,506</td>
</tr>
<tr>
<td>Bihar</td>
<td>94.16</td>
<td>8.30</td>
<td>10,286</td>
</tr>
<tr>
<td>Chhattisgarh</td>
<td>135.19</td>
<td>2.08</td>
<td>24,718</td>
</tr>
<tr>
<td>Goa</td>
<td>3.70</td>
<td>0.13</td>
<td>89,325</td>
</tr>
<tr>
<td>Gujarat</td>
<td>196.02</td>
<td>5.07</td>
<td>43,306</td>
</tr>
<tr>
<td>Haryana</td>
<td>44.21</td>
<td>2.11</td>
<td>53,661</td>
</tr>
<tr>
<td>Himachal Pradesh</td>
<td>55.67</td>
<td>0.61</td>
<td>41,973</td>
</tr>
<tr>
<td>Jammu &amp; Kashmir</td>
<td>222.24</td>
<td>1.01</td>
<td>26,081</td>
</tr>
<tr>
<td>Jharkhand</td>
<td>79.71</td>
<td>2.69</td>
<td>23,591</td>
</tr>
<tr>
<td>Karnataka</td>
<td>191.79</td>
<td>5.29</td>
<td>33,545</td>
</tr>
<tr>
<td>Kerala</td>
<td>38.86</td>
<td>3.18</td>
<td>39,315</td>
</tr>
<tr>
<td>Madhya Pradesh</td>
<td>308.25</td>
<td>6.03</td>
<td>19,108</td>
</tr>
<tr>
<td>Maharashtra</td>
<td>307.71</td>
<td>9.69</td>
<td>45,111</td>
</tr>
<tr>
<td>Manipur</td>
<td>22.33</td>
<td>0.23</td>
<td>25,059</td>
</tr>
<tr>
<td>Meghalaya</td>
<td>22.43</td>
<td>0.23</td>
<td>28,343</td>
</tr>
<tr>
<td>Mizoram</td>
<td>21.08</td>
<td>0.09</td>
<td>29,165</td>
</tr>
<tr>
<td>Nagaland</td>
<td>16.58</td>
<td>0.20</td>
<td>25,750</td>
</tr>
<tr>
<td>Orissa</td>
<td>155.71</td>
<td>3.68</td>
<td>23,227</td>
</tr>
<tr>
<td>Punjab</td>
<td>50.36</td>
<td>2.44</td>
<td>45,731</td>
</tr>
<tr>
<td>Rajasthan</td>
<td>342.24</td>
<td>5.65</td>
<td>22,563</td>
</tr>
<tr>
<td>Sikkim</td>
<td>7.10</td>
<td>0.05</td>
<td>34,821</td>
</tr>
<tr>
<td>Tamil Nadu</td>
<td>130.06</td>
<td>6.24</td>
<td>37,635</td>
</tr>
<tr>
<td>Tripura</td>
<td>10.49</td>
<td>0.32</td>
<td>30,527</td>
</tr>
<tr>
<td>Uttar Pradesh</td>
<td>240.93</td>
<td>16.62</td>
<td>16,880</td>
</tr>
<tr>
<td>Uttarakhand</td>
<td>53.48</td>
<td>0.85</td>
<td>32,113</td>
</tr>
<tr>
<td>West Bengal</td>
<td>88.75</td>
<td>8.02</td>
<td>30,744</td>
</tr>
<tr>
<td>All States</td>
<td>3276.28</td>
<td>101.21</td>
<td>28,693</td>
</tr>
<tr>
<td>Minimum</td>
<td>3.7</td>
<td>0.05</td>
<td>10286</td>
</tr>
<tr>
<td>Maximum</td>
<td>342.24</td>
<td>16.62</td>
<td>89,325</td>
</tr>
<tr>
<td>Max/Min</td>
<td>Rajasthan/Goa</td>
<td>UP/Sikkim</td>
<td>Goa/Bihar</td>
</tr>
</tbody>
</table>

**Source (Basic Data):** Report of the Twelfth Finance Commission and Central Statistical Organisation.
level of important public and merit services. Large differences induce migration from one state to another. It is the task of the Finance Commission to ensure that states are enabled to provide similar levels of services if they are willing to undertake similar levels of revenue effort.

1.3 Role of Finance Commissions

Fiscal transfers from the centre to the states in India are overseen by two major institutions: Finance Commission and Planning Commission. The Finance Commission looks after the current (revenue) account needs of the states while the Planning Commission is primarily concerned with the developmental needs of the states, which comprise both current and capital needs. The expenditure accounts of governments are further divided into non-plan and plan, and for the Finance Commissions with the exception of the First, Second, and Ninth, the ambit of concern has been limited to non-plan revenue (current) expenditures although there is no constitutional bar on their dealing with the full current account expenditures.

The duty of the Finance Commission, as enunciated in Article 280(3), relates to:

(a) the distribution between the Union and the States of the net proceeds of taxes which are to be, or may be, divided between them and the allocation between the States of the respective shares of such proceeds;

(b) the principles which should govern the grants-in-aid of the revenues of the States out of the Consolidated Fund of India;

(b) the measures needed to augment the Consolidated Fund of a State to supplement the resources of the Panchayats in the State on the basis of the recommendations made by the Finance Commission of the State;

(c) the measures needed to augment the Consolidated Fund of a State to supplement the resources of the Municipalities in the State on the basis of the recommendations made by the Finance Commission of the State; and

(d) any other matter referred to the Commission by the President in the interests of sound finance.

So far, Thirteen Finance Commissions have been constituted in India and Twelve have given their recommendations. The First Commission was constituted in 1951. The Thirteenth Finance Commission was constituted in 2007. The Finance Commission
generally makes recommendations that apply for five years, although there have been some exceptions. Table 1.2 gives the period of award of different Finance Commissions. It also provides a comparison of these award periods with the period covered by different five year plans.

**Source:** Report of the Eighth Finance Commission (P.122) for periods up to the Seventh Plan and subsequent announcements.

Notes: AP refers to annual plan.

Two issues that are critical for the consideration of the Finance Commission in this context relate to resolving the vertical and horizontal imbalances. The Finance Commission can

<table>
<thead>
<tr>
<th>Finance Commissions</th>
<th>Plans</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>No.</strong></td>
<td><strong>Period of Award</strong></td>
</tr>
<tr>
<td>First</td>
<td>1952-53 to 56-57</td>
</tr>
<tr>
<td>Second</td>
<td>1957-58 to 61-62</td>
</tr>
<tr>
<td>Fourth</td>
<td>1966-67 to 68-69</td>
</tr>
<tr>
<td>Fifth</td>
<td>1969-70 to 73-74</td>
</tr>
<tr>
<td>Sixth</td>
<td>1974-75 to 78-79</td>
</tr>
<tr>
<td>Seventh</td>
<td>1979-80 to 83-84</td>
</tr>
<tr>
<td>Eighth</td>
<td>1984-85 to 88-89</td>
</tr>
<tr>
<td>Ninth (1year award)</td>
<td>1989-90</td>
</tr>
<tr>
<td>Ninth (main award)</td>
<td>1990-91 to 94-95</td>
</tr>
<tr>
<td>Tenth</td>
<td>1995-96 to 99-00</td>
</tr>
<tr>
<td>Eleventh</td>
<td>2000-01 to 04-05</td>
</tr>
<tr>
<td>Twelfth</td>
<td>2005-06 to 09-10</td>
</tr>
</tbody>
</table>
use two instruments of transfers, viz., tax devolution and grants to resolve these imbalances. The vertical issue viz, the share of the states in Central resources, has to be considered on the basis of objective criteria and in the context of the overall transfers from the centre to the states. In the case of tax devolution, the horizontal dimension has so far been addressed, prior to the Report of the Eleventh Finance Commission, on a tax by tax basis. The principle of ‘return’ was earlier given some weight in the distribution of income tax while developmental needs including adequacy of provision of essential general, social, and economic services was given greater attention in the sharing of Union excise duties. Over time, however, a convergence became visible in the factors determining both sets of shares. A full convergence was achieved with the recommendations of the Eleventh Finance Commission where three sets of factors reflecting needs, costs disabilities, and fiscal performance, were used.

In relation to grants, duties of the Finance Commission are specified conjointly by Articles 280(3) / (b) and 275. Article 280(3) / (b) requires the Commission, to make recommendations as to the “principles” which should govern such grants-in-aid. Following from Article 275(1), specific “sums” are to be recommended to be paid to the States which are assessed to be in “need of assistance”. While Article 270 (sharing of central taxes) speaks of percentage share, Article 275 refers to specific ‘sums’. The Constitution prescribes that these grants are to be ‘charged’ on the Consolidated Fund of India, and have to be recommended by a Finance Commission.

1.4 Assignment of Resources and Vertical Imbalance

In India, as in most major federations of the world, the assignment of sources of revenues and responsibilities in the constitution is such that the central government has the larger share of resources and the states have the larger responsibilities. This creates a resource gap, called in the literature as the ‘vertical gap’. This vertical imbalance between resources and responsibilities of the central and the state governments is brought into balance by the process of transfers of resources from the central government, which has the excess resources, to the states, which have the excess responsibilities relative to their resources.

In the constitutional provisions, the vertical gap has been provided for by design. This is because in raising revenues, there is a need to obtain economies of scale and efficiency which is felicitated by uniform laws and harmonious tax rate structure
throughout the country so as to provide an integrated countrywide market. States are given a larger share of responsibilities because they can understand the local needs and conditions better, and can generally better reflect the preferences of the people living in their jurisdictions. The vertical imbalance should be resolved by transferring resources from the centre to the state governments in an objective and transparent manner. In addition, there is a horizontal imbalance, which arises because some states, compared to others, have larger resources due to a higher level of development and natural endowments. It is often the case as that states with larger needs have relatively less resources and the horizontal imbalance may be quite large. The horizontal imbalance can be resolved, by transferring relatively more to those states that have less resources and larger needs, so that certain minimum standards of important public and merit services can be ensured to all citizens. This equity objective should not lead to a methodology of transfers that gives rise to adverse incentives, such that states begin to depend on the central transfers rather than fully exploiting their own resource bases. The system of fiscal transfers in a federal system must resolve both the vertical and horizontal imbalances in a fair and equitable manner that does not compromise the efficiency of the system.

Thus, in the working of fiscal federal arrangements, two types of imbalances need to be resolved: vertical and horizontal. Determining the aggregate share of states (vertical transfers) in the central resource pool requires a comprehensive view of (i) the expenditure needs of the centre; (ii) the aggregate resources of the centre; (iii) the aggregate requirements of the states; and (iv) the total resources of states from own sources. In the context of vertical devolution, the share of states and consequently that of the centre is supposed to be determined in a manner that provides both sides with adequate resources subject to the overall resource constraint. Furthermore, in the determination of the vertical share, there needs to be adequate predictability and stability. Stability in the vertical transfers would enable both the centre and the states to plan their expenditures in a long-term perspective.

Since fiscal transfers take place through three channels in India, viz., Finance Commission, Planning Commission, and directly from the central government, these need to be put together in order to see the extent of vertical transfers. In Table 1.3, the aggregate transfer to the states through all channels has been indicated as percentage of the gross revenue receipts of the centre. Total transfers to states as percentage of centre's gross revenue receipts show some inter-year volatility. But this volatility is in a limited range.
Table 1.3
Transfers Relative to Centre's Gross Revenue Receipts and GDP

<table>
<thead>
<tr>
<th>Finance Commissions</th>
<th>Year</th>
<th>Total</th>
<th>Transfers Centre's Gross Revenue Receipts (CGRR)</th>
<th>GDPmp</th>
<th>Transfers as % of</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>CGRR</td>
</tr>
<tr>
<td>Eighth</td>
<td>1984-85</td>
<td>10830.35</td>
<td>29327</td>
<td>249268</td>
<td>36.93</td>
</tr>
<tr>
<td></td>
<td>1985-86</td>
<td>14046.56</td>
<td>35535</td>
<td>281330</td>
<td>39.53</td>
</tr>
<tr>
<td></td>
<td>1986-87</td>
<td>15515.59</td>
<td>41424</td>
<td>314816</td>
<td>37.46</td>
</tr>
<tr>
<td></td>
<td>1987-88</td>
<td>18238.68</td>
<td>46628</td>
<td>357861</td>
<td>39.12</td>
</tr>
<tr>
<td></td>
<td>1988-89</td>
<td>20372.63</td>
<td>54261</td>
<td>424532</td>
<td>37.55</td>
</tr>
<tr>
<td>Ninth</td>
<td>1989-90</td>
<td>21805.46</td>
<td>65329</td>
<td>487683</td>
<td>33.38</td>
</tr>
<tr>
<td></td>
<td>1990-91</td>
<td>26919.58</td>
<td>69531</td>
<td>569624</td>
<td>38.72</td>
</tr>
<tr>
<td></td>
<td>1991-92</td>
<td>32524.05</td>
<td>83227</td>
<td>654729</td>
<td>39.08</td>
</tr>
<tr>
<td></td>
<td>1992-93</td>
<td>38157.61</td>
<td>94639</td>
<td>752591</td>
<td>40.32</td>
</tr>
<tr>
<td></td>
<td>1993-94</td>
<td>43462.86</td>
<td>98024</td>
<td>865805</td>
<td>44.34</td>
</tr>
<tr>
<td></td>
<td>1994-95</td>
<td>45036.52</td>
<td>116160</td>
<td>1015764</td>
<td>38.77</td>
</tr>
<tr>
<td>Tenth</td>
<td>1995-96</td>
<td>50029.39</td>
<td>139269</td>
<td>1191812</td>
<td>35.92</td>
</tr>
<tr>
<td></td>
<td>1996-97</td>
<td>59396.67</td>
<td>162218</td>
<td>1378616</td>
<td>36.62</td>
</tr>
<tr>
<td></td>
<td>1997-98</td>
<td>68711.04</td>
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<td>3126596</td>
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<td>Averages</td>
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<td>Ninth</td>
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<tr>
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<td>2005-07</td>
<td></td>
<td></td>
<td></td>
<td>40.43</td>
</tr>
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</table>

Note: GDPmp: Gross Domestic Product at market prices.
Transfers as percentage of centre’s gross revenue receipts during the period 1984-85 to 2007-08 have ranged from a minimum of 33.2 per cent to a maximum of 44.3 per cent. However, considering Commission periods as a whole, there is some evidence that in the period covered by the Ninth Finance Commission the transfers were on an average close to 39.5 per cent and this percentage came down in the two subsequent Finance Commissions to a little above 35 per cent. Beginning with the Twelfth Finance Commission, the share of states in the centre’s gross revenue receipts has again come back to a level close to 40 per cent or above on an average.

The Eleventh Finance Commission, with a view to imparting greater stability and predictability to central transfers to states, had set out an “indicative” limit of 37.5 per cent of centre’s revenue resources for transfer to states through all modes of transfer. This benchmark limit was raised by the Twelfth Finance Commission to 38 per cent.

1.5 Devolution of Taxes: Major Recent Changes

Some major changes regarding sharing of central taxes and grants are discussed below.

a. Eightieth Amendment to Constitution

Until the year 2000, sharing of central taxes was on a tax by tax basis. In particular, two important central taxes were shared with the states, viz., (personal) income tax and the Union excise duties. Two important central taxes were not shared with the states, viz., corporation tax and custom duties. The Eightieth Amendment to the Constitution (May 2000, but effective from 1996-97) has put the sharing of central taxes with the states on an entirely new plane. Details are given at Annexure 1. With the amendment of the constitution, the net proceeds of all Union taxes and duties except central sales tax and consignment tax, surcharges on central taxes and duties, and earmarked cesses, are distributable between the centre and the states. The amendment is based on the alternative scheme of devolution that was recommended by the Tenth Finance Commission, in its report submitted in November 1994. The amendment has been brought about to serve the following main objectives:

1. Widening of the shareable revenue base for the states, thereby enabling them to
share the aggregate buoyancy of central taxes including that of the corporation tax;

2. Sharing of the burden of adjustment between the centre and the states in case of any temporary revenue erosion as a result of tax reforms;

3. Reducing the overall volatility in the growth of shareable revenues implicit in a larger shareable base; and

4. Providing an incentive for the exploitation of taxes mentioned in the existing Article 269 (except central sales tax and consignment tax) of the Constitution by including these in the shareable pool.

With this amendment to the Constitution, the share of the central taxes recommended for the states does not form part of the Consolidated Fund of India. It is implied in Article 270 that the same percentage share will apply to all central taxes that are to be shared. As discussed before, the sharing of central tax revenues with the states has both a vertical dimension, i.e., the aggregate share of the states in the central taxes, and a horizontal dimension, that is, the respective share of each state in the aggregate share of all states.

Prior to the 80th Amendment to the Constitution, the term “are to be” made reference to income tax other than corporation tax under Article 270, and the term “may be” made reference to the Union excise duties under Article 272. After the 80th Amendment, there are no taxes that “may be” shared between the centre and the states. Article 269 has also been amended and it contains only central sales tax and consignment tax. The latter has not been levied so far. Only “net proceeds” are to be shared, and as such ‘cost of collection’ has to be deducted to obtain the net proceeds as prescribed under Article 279 although the original recommendation by the Tenth Finance Commission was to provide for the sharing of ‘gross proceeds”. The proceeds are to be distributed among the states where the central taxes are “leviable” in “that year”.

b. Eighty-eighth Amendment to Constitution

The Eighty-eighth Amendment to the Constitution placed taxation of services under Article 268 by inserting a new Article 268A (details in Annexure 2). As part of Article 268, as provided in the Eightieth Amendment to the Constitution, service tax was taken
out of the scope of Article 270. It is therefore not subject to the mandatory sharing under the recommendation of the Finance Commission although the central government at its own discretion can allocate a share to the states and this share can be the same as for other central taxes under the recommendations of the Finance Commission. But qualitatively, the sharing of the service tax revenue is on a different footing as compared to the other central taxes.

1.6 Determination of Grants

a. Provisions of Article 275

Article 275(2) provides that “after a Finance Commission has been constituted no order shall be made under this clause (i.e., Article 275) except after considering the recommendations of the Finance Commission”. Article 275 stipulates that (i) these grants should be given to states which are in need of assistance, as Parliament may by law provide, and (ii) the different sums may be fixed for different states. As such, under constitutional provisions, only a Finance Commission can recommend grants under Article 275. Article 275 has two clauses. In the first clause, a distinction is made between its “substantive part” and the two “provisos”. In the course of its work, the Second Finance Commission (1957) considered the question as to whether their recommendations under Article 275(2) should cover not only the substantive portion of Clause (1) or these should also embrace its provisos. The majority of the Members in the Commission held the view that Clause (2) of Article 275 covered not only the substantive part of Clause (1) but also the two provisos thereunder. The matter was referred to the Ministry of Finance for clarification as to the interpretation, and the Ministry was requested that, if the interpretation of the Commission was acceptable to the President, or if the term of reference as it stood did not include the two provisos, as the case may be, the President be pleased to issue necessary orders to enable the Commission to make recommendations accordingly. The Ministry informed that the Commission’s duty was to make recommendations only in respect of grants-in-aid as to which Parliament could make a law under Clause (1) of Article 275. Further, as the provisos constituted exceptions to the main provision, there was no provision for Parliament making any law in these cases. Therefore, the Ministry of Finance conveyed to the Commission the decision of the President that the power of the Commission to make recommendations under Clause (2) did not extend to the grants under the two
provisos and remained limited to the substantive part of Para 1 of Article 275. With a view to avoid any ambiguity in the matter, the TOR to subsequent Commissions made a specific reference to the grants under Article 275 by inserting the words ‘for purposes other than those specified in the provisos to Clause (1) of that Article’.

The important issues that have concerned analysts are whether Article 275 grants should be given only to cover non-plan revenue expenditure rather than the entire revenue expenditure, and whether these can be given also to provide for some capital expenditure.

The Seventh Finance Commission (1978), while recommending grants-in-aid for upgradation of standards of administration, favoured giving grants for meeting capital expenditure as well. The Commission noted that the grants made under revenue account did not make adequate provision for administrative and residential buildings, and for uplifting standards of service capital grants were also needed. The Commission found that there was an implicit and inherent provision for making capital grants, notwithstanding the fact that the proviso was specifically outside the reach of the Commission, under the terms of reference. The Commission stated:

“We have given careful consideration to the scope for grants-in-aid under Article 275 for meeting capital expenditure. The operative part of this article speaks of “sums”. There is no restriction or bar in the article against making grants for capital expenditure. The first proviso of the article expressly speaks of grants of capital sums. This goes to show that the expression grants-in-aid of revenues do not limit grants to revenue expenditure only. We are fortified in this view by the Note of the Chairman of the Fourth Finance Commission appended to its Report on the interpretation of Article 275. Further, it seems unreasonable to hold that the operative part of the Article enables the Commission to make grants for revenue expenditure only, while the proviso enables grants being made for revenue as well as capital nature. It is quite clear therefore that it is open to us to recommend grants for capital expenditure also, apart from grants for revenue expenditure under Article 275” (Para 8 of Chapter 10 of the Report).

In principle, Article 275(1) makes no restriction as to whether needs should be considered on revenue account only. Furthermore, there is no stipulation that it should be restricted only to the non-plan revenue account. The next issue relates to whether the whole revenue
account or only the non-plan revenue account should be considered by the Finance Commission. There is no restriction in the constitutional provision in this regard. In fact, the term “grants-in-aid of the revenues” does not imply that consideration should only be of revenue expenditures, i.e., current expenditure. Revenues of the States are meant to be spent both on current and capital needs, and there is no constitutional restriction as to what needs should be considered and what should not be considered by the Finance Commission. Further, the distinction between plan and non-plan expenditures has not been made anywhere in the Constitution. Article 112 makes a reference to expenditure on ‘revenue’ account to be distinguished from ‘other’ expenditures.

b. Relative Scope of Articles 275 and 282

The distinction between non-plan versus plan revenue expenditure became material with a minute of dissent given by the Member-Secretary of the Third Finance Commission (1961). The Third Finance Commission took into account the needs of the States for the 3rd Five Year Plan and recommended by a majority that the quantum of grants-in-aid should be fixed in such a way as to enable the States, along with any surplus out of devolution, to cover 75 per cent of the revenue component of their plans. In determining the revenue component, the Commission deducted the amount of additional tax to be raised by each State as incorporated in the plan itself. The Commission also recommended special grants to 10 States for the improvement of communications. The recommendations on the first item, were not accepted by the President but those on the second, were accepted. Ashok Chanda, Chairman of Third Finance Commission, observed: “…the Planning Commission did not take kindly to the basic scheme or suggestions of the Commission. It was not unexpected therefore that the Member-Secretary of the Commission who was an official, should take the unusual step of appending a note of dissent, nor was it strange that government used this note for rejecting this particular recommendation” (Federalism in India: 1965, p. 222).

The Ninth Finance Commission had formally consulted some well known authorities to take their views as to the relative scope of Articles 275 and 282. Summarizing their views that differed from each other, the Ninth Finance Commission had observed that “…we are quite certain that if our constitutional obligations under Article 280 read with Article 275 require us to enlarge the scope of grants beyond the non-plan account, we should not hesitate to do so.” The Commission had then proceeded to recommend grants for
plan purposes under Article 275. In other words, the Finance Commission can and has often given grants under Article 275 for the entire revenue account covering both plan and non-plan revenue expenditure. It has also given grants for capital expenditure.

c. Grants for Local Bodies

Another area where Article 275 grants have been used is to provide support for the rural and urban local bodies. The terms of reference to the Finance Commission since the Eleventh Finance Commission also make reference to the local bodies. This derives from Article 280(3) (bb) and (3) (c), which was inserted in this article after the 73rd and 74th Amendments to the Constitution, relating respectively to the resources of panchayats (rural local bodies) and municipalities (urban local bodies). The Constitution requires the Finance Commission to make recommendations regarding the “measures” needed to augment the Consolidated Funds of States to supplement the resources of the panchayats and municipalities, respectively. These “measures” do not necessarily imply that grants should be provided, although such grants could be one of many such measures, and could also serve to induce other measures.

The Terms of Reference of the Finance Commissions beginning from the Eleventh Finance Commission have provided that the Finance Commission should make its recommendations on the “basis of the recommendations by the Finance Commission of the State”. The State Finance Commissions (SFCs) have had heterogeneous approaches, methodologies, and time periods.

In the context of resource transfers, three important issues for the consideration of the Commission relate to determining: (i) the size of overall transfers relative to Centre’s gross revenue receipts, (ii) the appropriate ratio between tax devolution and grants in the overall transfers recommended by Finance Commission, and (iii) the relative shares of general purpose and conditional grants in total grants.

1.7 Summary

In this Chapter, we have examined the scope of the term of reference to the Commission
on Centre and State Relations regarding the impact of the recommendations made by the Eighth to the Twelfth Finance Commissions on the fiscal relations between the centre and the states. The TOR makes reference to the dependence of the states on devolution of funds from the centre. It seems to assume that this dependence has become greater over time. We have argued that the dependence of the states on devolution of funds from the centre may be measured by the share of such devolution in the states’ total revenue receipts. We have further argued that even if there is no clear evidence of increasing dependence of the states on devolution of funds from the centre, the term fiscal relations should be interpreted in a broad manner covering both quantitative and qualitative aspects of fiscal transfers. In particular, fiscal relations can be considered to be healthy and efficient if the states maintain sufficient autonomy with regard to expenditures undertaken by them on items listed in the state list and there is no over-centralisation of either the revenue or the expenditure space. Wherever there are vertical externalities affecting the revenue and expenditure decisions of one tier of government by the other tier of government, fiscal relations are best served by processes of mutual consultations or joint decision making.

Two major amendments to the Constitution affecting the tax devolution process since the period of the Eighth Commission were the 80th and the 88th Amendments to the Constitution. The 80th Amendment brought all central taxes excluding Articles 268 and 269 taxes under Article 270 for sharing with the states under recommendations of the Finance Commissions. The 88th Amendment however placed the service tax outside of this generalized arrangement of sharing. In addition, the central government also began to rely relatively more on cesses and surcharges. In relation to grants there has been a debate regarding the scope of Article 275 and 282 and the links between grants given by the Finance Commission and the assistance given by the Planning Commission to the states.

In the next Chapter, we consider the evolution of the principles of transfers by the Finance Commission as well as the Planning Commission regarding tax devolution as well as grants with a view of highlighting those features that may result in increased dependence of states on devolution of funds from the centre.
Finance Commissions: Approach to Determining Devolution of Funds

As discussed in Chapter 1, the Finance Commission recommends transfers to the states under two modes of transfers (a) share in central taxes, and (b) grants under Article 275. The principles of transfers as adopted by different commissions have been different for these two channels of transfers. In so far as determining the inter se shares of states in central taxes are concerned, the Finance Commission has followed a formula based approach using a set of criteria. These criteria and the weights attached to the respective criteria have changed over time. These are reviewed in this Chapter. Further, grants under Article 275 have generally been unconditional grants. The unconditional grants have often been called as revenue-gap grants. The Finance Commissions have often been criticized for following what is known as the gap-filling approach in the determination of the revenue gap grants. There have also been other grants, which have been earmarked for use for specific purposes. For other grants, different considerations have been used. In this Chapter, we will review the criteria for determination of states' share in central taxes as well as those for grants focusing on the period covered by the Eighth Finance Commission onwards.

2.1 Evolution of Tax Revenue Sharing Criteria

In reviewing the inter se distribution of the aggregate share of states in central tax revenues, the approach of the Finance Commissions can be studied in terms of their approach prior to the 80th Amendment and that after it. Up to the Seventh Finance Commission, the distribution formulae used for determining the income tax shares were clearly distinct from those for the Union excise duties and were given under two separate Articles of the Constitution, viz., Article 270 and Article 272. Article 270 had provided for a mandatory sharing of income tax while Article 272 had provided for the sharing of the Union excise duties at the discretion of the
centre. From the Eighth Finance Commission, a process of convergence between the two sets of formulae began. A full convergence was arrived at with the recommendations of the Eleventh Finance Commission, after the 80th Amendment based on the recommendation of the Tenth Finance Commission.

a. **Sharing of Income Tax and the Union Excise Duties: Eighth to Tenth Finance Commissions**

Prior to the 80th Amendment to the constitution, income tax and Union excise duties were shared with the states under two different articles of the Constitution although broadly the factors were the same, namely, population, some index of backwardness, and collection or contribution. In determining the inter se shares, even when the factors were the same, the weights were different. There were also some factors that were used specifically for one tax. With the Eighth Finance Commission, two changes occurred. First, there was a move towards unifying the formulae for the inter se distribution of both income tax and Union excise duties and, secondly, a portion of the Union excise duties was kept aside for distribution according to 'assessed deficits'. There was a large portion of the shareable part of revenues, both for income tax and Union excise duties, which was subjected to a common unified criterion. Table 2.1 gives the unified formulae used by the Eighth, Ninth and Tenth Commissions. The weight to the factor of population has ranged between 20 to a little less than 30 per cent for different Commissions.

The sharing of portions that were kept out of the unified formula was done as follows. In the case of income tax, 10 per cent of the share recommended for the states was to be shared on the basis of assessment of income tax (Eighth and Ninth Finance Commissions). In the case of Union excise duties, a portion of the shareable proceeds for devolution was kept aside for distribution among states on the basis of assessed deficits. The share kept aside for this purpose also gradually increased. It was 5 percentage points out of 45 per cent of the shareable proceeds of Union excise duties, which formed the states' share, in the case of Eighth Commission and the First Report of the Ninth Commission. It was raised to 7.425 percentage points in the case of the Second Report of the Ninth Commission and subsequently to 7.5 percentage points out of 47.5 per cent of the shareable proceeds of the Union excise duties by the Tenth Commission.
Table 2.1

*Inter se Sharing of Income Tax and Union Excise Duties*: Phase II: Eighth, Ninth and Tenth Finance Commissions

A. Sharing of 90 per cent of divisible pool of Income Tax and specified portion of divisible pool of Union Excise Duties according to Common Criteria

<table>
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<tr>
<th>Finance Commission</th>
<th>Criteria</th>
<th>Population</th>
<th>Distance</th>
<th>Inverse Income</th>
<th>Poverty Ratio</th>
<th>Index of Backwardness</th>
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<tbody>
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<td>Eighth</td>
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<td>50</td>
<td>12.5</td>
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<td>12.5</td>
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<tr>
<td>Ninth (2) Union Excise Duties</td>
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<td>29.94</td>
<td>40.12</td>
<td>14.97</td>
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<td>Tenth</td>
<td></td>
<td>20</td>
<td>60</td>
<td>5</td>
<td>5</td>
<td>10</td>
</tr>
</tbody>
</table>

B1. Income Tax: Sharing of Balance Amount

**Eighth and Ninth Finance Commissions**: Sharing of 10 per cent of divisible pool of income tax: According to assessment/contribution. **Tenth Finance Commission**: The balance 10 per cent was also distributed according to criteria given in Part A of the Table.

B2. Union Excise Duties: Sharing of Balance of Divisible Amount

**Eighth and Ninth Finance Commissions (First Report)**: 5 percentage points out of 45 per cent of Union Excise Duties, which formed the States’ share, according to assessed deficits.

**Ninth Finance Commission (Second Report)**: 7.425 percentage points out of 45 per cent according to assessed deficits.

**Tenth Finance Commission**: 7.5 percentage points out of 47.5 per cent according to assessed deficits.

**Source**: Reports of Finance Commissions, Government of India.

Prior to the 80th Amendment, apart from the two main taxes, viz., income tax and the Union excise duties, two other arrangements for transfers were in vogue, viz., grant in lieu of tax on railway passenger fares and additional excise duties in lieu of sales tax on specified commodities (cotton textiles, tobacco and sugar). Both of these arrangements were tax rental arrangements in the sense that the original power to levy the tax was
vested with the state governments but were transferred to the centre for the sake of uniformity across states among other reasons. With the 80th Amendment to the Constitution, the separate identity of these arrangements was also abolished.

b. Sharing of All Central Taxes: Alternative Scheme of the Tenth to Twelfth Finance Commissions

Under the new provisions following the 80th Constitutional Amendment, only one set of shares is to be determined replacing four distinct sets, which were needed prior to relating respectively to (i) portions of income tax and Union excise duties subjected to common criteria; (ii) portion of devolution according to assessed deficits; (iii) grant in lieu of tax on railway passenger fares; and (iv) additional excise duties in lieu of sales tax on cotton textiles, tobacco and sugar. The criteria followed by the Tenth Finance Commission (Alternative Scheme), and the subsequent Commissions relate to this generalised sharing arrangements. These criteria jointly reflect four considerations: (i) vertical transfers, (ii) horizontal equity, (iii) incentives for efficiency, and (iv) cost disadvantages.

Two core criteria, which have been used by the Finance Commissions for horizontal equity, providing higher per capita transfers to lower per capita fiscal capacity states, are distance and inverse-income formulae. In the case of the Eighth Finance Commission, the combined weight given to these two criteria was 75 per cent. In the

### Table 2.2
Criteria and Relative Weights for Determining *Inter se* Shares of States

<table>
<thead>
<tr>
<th>Criteria</th>
<th>Relative Weight (Per cent)</th>
</tr>
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<tr>
<td>1. Population</td>
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<td>2. Distance</td>
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<td>3. Area</td>
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<tr>
<td>4. Index of Infrastructure</td>
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<td>5. Tax Effort</td>
<td>10.0</td>
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<tr>
<td>6. Fiscal Discipline</td>
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</table>

Source: Reports of Finance Commissions, Government of India.
case of the Ninth Finance Commission (Second Report), the combined weight for these two criteria was 62.5 per cent for income tax. An additional equity related criterion was used in the form of the index of backwardness (replacing the index of poverty used in the First Report), which was given a weight of 12.5 per cent. The weight of these three equity related criteria added to about 70 per cent in the case of Union excise duties. The Tenth Finance Commission had decided to use only one of these criteria, namely, the distance formula and gave it a weight of 60 per cent. The Eleventh Finance Commission had kept the weight to this criterion at 62.5 per cent.

Table 2.2 gives the different criteria and related weights followed by the Tenth (Alternative Scheme), Eleventh, and Twelfth Finance Commissions.

These Finance Commissions had also endeavored to evolve a structure of incentives in the mechanism of fiscal transfers. The Tenth Finance Commission had utilised an index of tax effort made by the states. The Eleventh Finance Commission had utilised an index of tax effort and an index of fiscal discipline, and given these a combined weight of 12.5 per cent. The Twelfth Finance Commission gave a combined weight of 15 per cent to these two criteria. In the index of fiscal discipline, the improvement is measured by considering the ratio of the measure of fiscal discipline in a reference period in comparison to a base period. Another relativity was to look at the state-specific improvement with respect to the average improvement. Higher own revenues or lower revenue expenditures or any combination of the two can bring about an improvement in fiscal self-reliance. Further, the state specific improvements are related to the corresponding all state improvement to neutralise factors that commonly affect all states. The comparison of the performance of a state with the all-state performance reflected the consideration that if the revenue performance of states is deteriorating in general, the state that accomplishes a relatively lower deterioration is to be rewarded relatively more than average. Similarly, if all revenue balance profiles are improving, the state where improvement is relatively more than average is rewarded relatively more.

Cost variations were also brought into consideration through the criteria based on area and index of infrastructure: larger the area (per crore population), higher the per capita cost; similarly, lower the index of infrastructure, higher is the per capita cost. Thus, the three main considerations in the selection of criteria used by the Tenth (Alternative Scheme), Eleventh, and Twelfth Finance Commissions relate to: (i) resource deficiency, (ii) higher cost of providing services, and (iii) fiscal discipline.
2.2 Determination of Grants

Under the provisions of this Article 275, the main unconditional grant is the 'revenue-gap' grant. The Finance Commissions make an assessment of expenditures of each state on revenue account (non-plan or total) as also an assessment of states' own revenues. Once tax devolution to each state has been determined, grants-in-aid are determined as a residual. It is the difference between the assessed expenditure and the sum of the projected own revenues and shares in central taxes. Thus, the 'revenue-gap' grants under the Finance Commission are meant to finance that part of expenditure, which is not covered by the sum of own revenues and share in central taxes. This procedure, many people argue, gives rise to adverse incentives. The main issue here is as to whether this gap should be projected on the basis of historical trends or by an assessment of expenditures and revenues on a normative basis. If historical basis is followed, it will give rise to strong adverse incentives where it will be to the benefit of each state to maximize their histories of expenditures and minimize their histories of raising revenues. On the other hand, if the gap is determined strictly on a normative basis, such an adverse incentive will not be present.


In the case of grants, the First Finance Commission had set out some first principles for determining grants-in-aid. Its recommendations were as follows:

a. Budgetary Needs: The Commission observed that budgetary need (s) is an important criterion for determining ... of the amount of the grants-in-aid, ..... , several adjustments are however necessary ...... (to) to reduce all budgets to a comparable basis.

b. Tax Effort: The Commission observed that it is not enough to just consider the comparative poverty or affluence of the states as judged by indices of their relative per capita incomes but it is also important to take into account the relative tax efforts of the states. This seems to the first mention of normative principle where fiscal capacity and tax effort are mentioned as key determinants of grants-in-aid.

c. Economy in Expenditure: The Commission observed that allowance should be made for possibilities of economy in expenditure. The Commission observes that "the method of extending Finance Commission Assistance should be such as to avoid any suggestion that the Central Government have taken upon
themselves the responsibility for helping the states to balance their budgets from year to year. If the amount of grants-in-aid were to be merely in proportion to the financial plight of a state, a direct premium may be placed on impecunious policies and a penalty imposed on financial prudence". This seems to be the first clear and explicit caution against following any gap filling approach.

d. Standard of Social Services: The Commission observes that "an important purpose of grants-in-aid is to help in equalizing standards of basic social services". This is the first mention of equalization in respect of basic social services.

e. Special Obligations: The Commission mentioned that certain states may have special obligations or burdens that are likely to continue for a period of years, i.e. commitment arising out of abnormal conditions. They mention as examples of abnormal conditions: strain on the economy and administration and increase responsibility with respect of security.

f. Broad Purposes of National Importance: The Commission favored that grants may be given to further any service of primary importance in which it is in the national interest to assist the less advanced states.

It is clear therefore, that the First Finance Commission explicitly stated the best theoretically accepted principles that had emerged in literature for guiding the determination of fiscal transfers.

b. Terms of Reference and Grants

An important reason for the Finance Commissions for following the kind of methodology emanates from the considerations listed in the Terms of Reference (TOR). A typical para in the TOR of the Finance Commissions makes reference to the resources of the central government and the demands on those resources. The TOR generally provides that resources of the central government have to be assessed on the basis of levels of taxation and non-tax revenues likely to be reached at the end of a specific base year. A reference of this nature has been made to successive Finance Commissions since the Fifth Finance Commission. A similar reference to a base year is made in the case of the states.

With the 'base year' being part of the TOR, the methodology followed by the Finance Commission builds up projections on the base year. Although most of the recent
Commissions have made an attempt not to simply use historical growth rates of revenues or expenditures in their assessments, the assessments are still driven by a number of historical parameters, which are often subjected to modifications with a view to introducing an element of prescriptive benchmarks or norms. An explicit reference as to the use of a normative approach was made only for the Ninth Finance Commission by including in the TOR the following:

"In making its recommendations, the Commission shall:

(i) adopt a normative approach in assessing the receipts and expenditures on the revenue account of the States and the Centre and, in doing so, keep in view the special problems of each State, if any, and the special requirements of the Centre such as defence, security, debt servicing and other committed expenditure or liabilities;

(ii) have due regard to the need for providing adequate incentives for better resource mobilization and financial discipline as well as closer linking of expenditure and revenue raising decisions;

(iii) take into account the need for speed, efficiency and effectiveness of Government functioning and of delivery systems for Government programme; and

(iv) keep in view the objective of not only balancing the receipts and expenditure on revenue account of both the States and the Centre, but also generating surpluses for capital investment …"

A direct reference to a normative approach in the TOR has not been made for the subsequent Commissions. In their cases, the typical para in the TOR has reverted back to the reference of the base year.

c. Gap-Grants and Normative Approach

From a methodological view point, the determination of the so called revenue-gap grants is the most important. It is in this context that the Finance Commissions have often been accused of following a gap filling approach, which leads to significant adverse incentives. Grants-in-aid under the Finance Commission are meant to fill up a 'gap' which represents expenditure not covered either by own revenues or share in central taxes. The main issue here is as to whether this gap should be projected on the basis of historical trends or by an assessment of expenditures and revenues on a
normative basis. It is clear that if historical basis is followed it will give rise to strong adverse incentives where it will be to the benefit of each state to maximize their histories of expenditures and minimize their histories of raising revenues. On the other hand, if the gap where to be determined strictly on a normative bases, such an adverse incentive will not be present.

As mentioned, apart from the Ninth Finance Commission, no other Commission was formally asked in its TOR to follow a normative approach. Nevertheless Ninth Commission onwards, all Commissions have not followed an approach that may be called as simple projection of historical trends of revenues and expenditures. All the Commissions have imposed some norms of performance in regards to both tax and non-tax revenues and also used adjustments in the historical pattern of expenditures emphasizing more the need for increasing the priorities for expenditures on merit services like health and education as also capital expenditures while prescriptive adjustments were made leading to taking reduced or adjusted amounts in the case of interest payments, salaries and pensions. In most cases, these normative or prescriptive adjustments related to growth of revenues or expenditures and not so much in the base year figures but the base years figures were also adjusted.

The necessity for settling on a base year also arose from the way the TOR were designed. For example for the Twelfth Finance Commission, Para 6(i) and (ii) of the TOR of the Commission made reference to the resources of the central government and the demands on those resources and that such resources have to be assessed on the basis of "levels of taxation and non-tax revenues likely to be reached at the end of 2003-04". The 2003-04 tax and non-tax revenues were meant to serve as the base for assessment of resources for the period from 2005-06 to 2009-10.

The TORs also left an asymmetry between the way the needs to the central and state governments were referred to. For example, consider the references to the Twelfth and Thirteenth Finance Commissions:

Twelfth Finance Commission: Excerpts from Para 6 of the TOR

In making its recommendations, the Commission shall have regard, among other considerations, to:

(i) the resources, of the Central Government for five years commencing on 1st April 2005, on the basis of levels of taxation and non-tax revenues likely to be reached at the end of 2003-04;
(ii) the demands on the resources of the Central Government, in particular, on account of expenditure on civil administration, defence, internal and border security, debt-servicing and other committed expenditure and liabilities;

(iii) the resources of the State Governments, for the five years commencing on 1st April 2005, on the basis of levels of taxation and non-tax revenues likely to be reached at the end of 2003-04.

Thirteenth Finance Commission: Excerpts from Para 3 of the TOR

In making its recommendations, the Commission shall have regard, among other considerations, to:-

(i) the resources of the Central Government, for five years commencing on 1st April 2010, on the basis of levels of taxation and non-tax revenues likely to be reached at the end of 2008-09;

(ii) the demands on the resources of the Central Government, in particular, on account of the projected Gross Budgetary Support to the Central and State Plan, expenditure on civil administration, defence, internal and border security, debt-servicing and other committed expenditure and liabilities;

(iii) the resources of the State Governments, for the five years commencing on 1st April 2010, on the basis of levels of taxation and non-tax revenues likely to be reached at the end of 2008-09.

In both cases, there is a reference to a base year and the need to restrict the Finance Commission to consider 'levels' of taxation and non-tax revenues reached up to base years (leaving an growth in revenue during the assessment period based on 'additional resource mobilization' for the Planning Commission, presumably). Furthermore, while there is some mention of preemptive needs of the central government, there is no corresponding mention of the needs of the state governments.

2.3 Determination of Plan Grants

The second main mechanism of resource transfer in India is through the Planning Commission. The Planning Commission oversees grants meant for developmental expenditures of the states. The Planning Commission provides developmental grants to states as part of an overall assistance package. This package is determined as a composite
of loans and grants. The relative ratios of loans and grants are different for the special
category states as compared to the general category states. For the general category states,
assistance is 30 per cent grant and 70 per cent loan. For the special category states, 90 per
cent of assistance is given as grant and 10 per cent as loan. The expenditure side of state
budgets may be divided into four parts: non-plan revenue expenditure, plan revenue
expenditure, plan capital expenditure, and non-plan capital expenditure. The first and
second components combine to give the revenue account of a state, which pertains to
recurrent (revenue) expenditures. Plan assistance is meant for the second and third
components taken together. In the initial stages, when plan assistance was conceived of
in terms of an overall package, the expectation was that nearly 30 per cent of the plan
would actually be in the nature of recurrent expenditures and 70 per cent would pertain
to capital expenditures. In accordance with such an expectation, the grant to loan ratio in
plan assistance was fixed as 30 and 70 per cent of total plan assistance. It was expected
that all capital expenditures would be met by borrowing and by surpluses on revenue
account. As such no capital grants were envisaged for the general category of states in
plan assistance.

The position of the special category states was different in the sense that from the 90 per
cent that they were getting as grant, 30 per cent could be allocated for the revenue
component of the plan, and the balance of 60 per cent could then emerge as a capital
grant. In practice however the relative claim of recurrent expenditure continued to
increase and has become on an average 60 per cent of plan outlay in the case of
general category states. Borrowing thus basically finances capital expenditure, in the
general category states. In fact, it is not only that there are no capital grants, but also
a substantive part of current expenditures is being financed by borrowing.

The system of allocation of plan assistance from the centre to the states underwent a
basic change with the Fourth Five Year Plan. Until then, plan assistance was on the
basis of plan scheme projects, which allowed for considerable room for ad hocism.
States were calling for the formulation of some objective criteria for the allocation of
plan assistance. The National Development Council meeting in May 1968 decided
that an objective criteria for allocation of plan assistance to the states should be
formulated and set up a committee of Chief Ministers with Dr. D. R. Gadgil, the then
Deputy Chairman of the Planning Commission as its Chairman. The deliberations
of this committee led to the formulation of what came to be known as the Gadgil Formula.
The formula was adopted in September 1968. Since then, it has undergone three revisions. As such, we have had four mutations of the Gadgil Formula.

The Gadgil Formula is applied to state plan assistance, although states also receive allocations under central sector plan and centrally sponsored schemes. The changeover to the Gadgil Formula also brought an end to scheme-based allocations for plan assistance. Instead, the system of block assistance was evolved which led to the loss of link between plan assistance and plan projects/schemes.

Under the Gadgil Formula, since its first revision (1980), in the first stage, 30 per cent of total plan assistance is set apart for the special category states. It is not clear as to how this 30 per cent figure was arrived at. The original formulation in September 1968 had stipulated that out of the central assistance, a lump sum was to be set apart for first meeting the requirements of Assam, Jammu & Kashmir and Nagaland. In the Fifth Plan, again a provision was made to set apart a portion of central plan assistance for the state plans for the requirements of Assam, Himachal Pradesh, Jammu & Kashmir, Nagaland, Manipur, Meghalaya, Sikkim, and Tripura. Later the number of special category states was raised to 10. Since 1980, with the modified Gadgil Formula, a figure of 30 per cent as the share of special category states was formalised. However, it excluded the share for the north eastern council. Since 1990, the 30 per cent share also included the share of the north eastern council. The overall dispensation of (normal) plan assistance can be summarised according to special and non-special category states, and according to grants and loans as indicated in Table 2.3. Two other channels of plan assistance are additional central assistance (ACA) and external assistance. Both are given on the same terms and conditions as normal plan assistance.

Table 2.3
Dispensation of Plan Assistance: Normal State Plan  
(Per cent)

<table>
<thead>
<tr>
<th>States</th>
<th>Grants</th>
<th>Loans</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Special</td>
<td>27</td>
<td>3</td>
<td>30</td>
</tr>
<tr>
<td>General</td>
<td>21</td>
<td>49</td>
<td>70</td>
</tr>
<tr>
<td>Total</td>
<td>48</td>
<td>52</td>
<td>100</td>
</tr>
</tbody>
</table>

Source: Planning Commission.

The Planning Commission allocates aggregate (normal) plan assistance among states under
Table 2.4
Gadgil Formula: Alternative Versions
(Weightage Per cent)

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>A. Special Category States (10)</td>
<td>30% share of 10 States excluding North Eastern Council</td>
<td>30% share of 10 States including North Eastern Council</td>
<td>30% share of 10 States excluding North Eastern Council</td>
</tr>
<tr>
<td>B. Non-Special Category States (15)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(i) Population (1971)</td>
<td>60.0</td>
<td>55.0</td>
<td>60.0</td>
</tr>
<tr>
<td>(ii) Per Capita Income</td>
<td>20.0</td>
<td>25.0</td>
<td>25.0</td>
</tr>
<tr>
<td>Of which</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>a. According to the ‘deviation’ method covering only the states with per capita income below the national average</td>
<td>20.0</td>
<td>20.0</td>
<td>20.0</td>
</tr>
<tr>
<td>b. According to the ‘distance’ method covering all the fifteen states</td>
<td>-</td>
<td>5.0</td>
<td>5.0</td>
</tr>
<tr>
<td>(iii) Performance</td>
<td>10.0</td>
<td>5.0</td>
<td>7.5</td>
</tr>
<tr>
<td>Of which</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>a. Tax effort</td>
<td>10.0</td>
<td>-</td>
<td>2.5</td>
</tr>
<tr>
<td>b. Fiscal management</td>
<td>-</td>
<td>5.0</td>
<td>2.5</td>
</tr>
<tr>
<td>c. National objectives</td>
<td>-</td>
<td>-</td>
<td>2.5</td>
</tr>
<tr>
<td>(iv) Special problems</td>
<td>10.0</td>
<td>15.0</td>
<td>7.5</td>
</tr>
<tr>
<td>Total</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
</tr>
</tbody>
</table>

Notes:
1. Fiscal management is assessed as the difference between states’ own total plan resources estimated at the time of finalising Annual Plans and their actual performance, considering latest five years.
2. Under the criterion of the performance in respect of certain programmes of national priorities the approved formula covers four objectives, viz: (i) population control; (ii) elimination of illiteracy; (iii) on-time completion of externally aided projects; and (iv) success in land reforms.
a set of criteria called the Gadgil Formula. The original formula has been subjected to changes from time to time and the present version is referred to as the National Development Council (NDC) revised Gadgil Formula. As noted, the Gadgil Formula works in two stages. First, 30 per cent of total assistance money is earmarked for the special category states. This is distributed among these states on the basis of their plan size and past plan expenditures, without using any explicit criteria. The remaining 70 per cent are distributed among the general category states according to a set of criteria with relative weights. These criteria have been summarised in Table 2.4. A comparison can also be made between the alternative versions of the formula, as it has changed over time. The Planning Commission does not publish the actual shares of states either criteria-specific or aggregate as is done by the Finance Commission. The shares may change under each criterion, as more recent data on income, tax effort, etc., become available. However, as far as population is concerned, only 1971 population is used.

The important elements in this formula relate to factors of population, deviation of income from mean income, distance of income from highest income, and other factors reflecting fiscal discipline and achievement of national objectives. Due to the very high weight given to the population factor, which allocates equal per capita shares to all states, dispensations under the Gadgil Formula are only mildly progressive. As argued in a later chapter, whatever little progressivity is there in the plan transfer, it gets disturbed by the inter-state distribution of external assistance.

The main weaknesses in the application of the Gadgil Formula in its various mutations are summarised below:

i. There is no explicit basis for a 30 per cent earmarking for the special category states; it is way beyond their capacity to productively absorb these funds, and has led to large debt-GSDP ratios even while only 10 per cent of assistance is given as loan;

ii. Shares determined on the basis of tax effort and fiscal discipline indexes are unscaled implying that if a large state like Maharashtra and a small state like Goa had the same tax effort ratio, they will get the same share regardless of their size. This would lead to a very large per capita share for Goa compared to that for Maharashtra, for example, for the same tax effort;

iii. The link between plan schemes/projects and plan assistance has been lost, leading
to a severing of a link between costs and benefits, and lack of effective project based monitoring;

iv. The 30:70 grants to loan ratio has long become irrelevant if the 30 per cent grant ratio was meant to cover revenue expenditure on plans; and

v. There are no objective criteria for the distribution of 30 per cent earmarked share among the special category states.

The Twelfth Finance Commission had recommended that the link between the plan grants and plan loans should be discontinued. It has observed as follows1. The Commission recommended that (para 10.4 of the Report) "the system of imposing a 70:30 ratio between loans and grants for extending plan assistance to general category states (10:90 in the case of special category states) should be done away with. Instead, the Planning Commission should confine itself to extending plan grants to the states, and leave it to the states to decide how much they wish to borrow and from whom, i.e., from the centre or from the open market". The Commission was of the view that this "dis-intermediation" of the centre in the borrowing process of the states would ensure greater fiscal discipline on the part of the states by removing the structural obligation to borrow from the centre.

2.4 Finance and Planning Commissions: Dynamics of Inter-Dependence

The two main bodies that intermediate between the centre and the states in the matter of fiscal transfers, viz., the Finance Commission and the Planning Commission follow approaches in a segmented way without any effective coordination. Especially important in this context is the impact of the dynamic linkage between the two major streams of resource transfers.

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1 At present, the normal central assistance and the additional central assistance are given to the general category states by the centre in the form of 70 per cent loan and 30 per cent grant (10 per cent loan and 90 per cent grant in the case of special category states). This means that if a general category state wants a grant of Rs.30 from the centre, it must necessarily borrow Rs.70 from the same, and that, too, at a rate of interest which is often higher than the open market rate. It is also well known that the existing plan process inherently encourages ever larger plan sizes. All these result in states getting deeper into debt on account of structurally mandated borrowings. There is indeed no reason why plan grants to states should be linked to compulsory loans from the centre. The considerations that go into deciding the grants are, and should be, different from those relating to loans. Since almost the entire expenditure on plan is met by the centre from borrowed funds, central loans as part of the plan assistance unnecessarily increase the fiscal deficit of the centre (on a stand-alone basis).
The Plan generates three major liabilities for periods beyond the Plan: interest payments on funds borrowed for financing the Plan, maintenance of assets created during the Plan, and salaries of people employed in Plan schemes who remain in government employment after the plan has ended. For these liabilities, after the Plan period is over, state governments look to the Finance Commission for resource transfers. In making an assessment of the needs of state governments on the revenue (non-Plan) account, both interest payments and committed liabilities of the state governments have been taken into account by the Finance Commissions. Since the Plan is linked to a programme of borrowing, a larger Plan is typically linked with a larger borrowing programme and therefore, leaves relatively larger future liabilities.

Interest liabilities as well as committed expenditures on Plan schemes of the past have been taken by the previous Finance Commissions as a first charge in making an assessment of the expenditure requirements. Given other things, the larger the interest and other committed liabilities, the larger would be the entitlement of a state in the form of tax devolution and grants. It is implicit in this approach that larger Plan outlays financed by larger borrowing, create larger state-specific liabilities which generate (i.e., after five years) larger claims for fiscal transfers.

The methods of working out transfers by the Planning Commission and the Finance Commission thus sets up a circuit of adverse incentives, because in both cases, a fragmented view is taken, without addressing the issue in its totality. The Finance Commission keeps looking only to the (non-Plan) revenue expenditures without paying much attention to the linkage of interest payments with past fiscal deficits and accumulated debt stock. The Planning Commission looks only at new schemes. It looks at the scope of borrowing in the Plan period without considering what future liabilities are being created and how they may be financed beyond the Plan period. Projects financed by external assistance, which is transmitted to the state on the same terms and conditions as normal Plan assistance, also create similar liabilities regarding interest payments and maintenance.

By mixing grants and loans, the Plan assistance mechanism combines two modes of resource transfer, which need to be governed by entirely different sets of principles. Grants should be given in consideration of resource deficiencies, and for projects with large social benefits but limited direct return like primary education and primary health. On the other hand, loans should be given taking into consideration the capacity
of a state to absorb and service the loan, and in respect of projects which can give adequate returns, commensurate with the cost of the loan. By mixing the two together, the centre is burdening states with debt that they cannot service, but cannot afford to forego either, because with it the component of grant will also have to be foregone.

The artificial dichotomy between Plan and non-Plan expenditures also induces a number of inefficiencies. There is an undue emphasis on taking up new schemes, while uncompleted projects of the past Plans and maintenance of assets acquired in the past get little attention. In effect, Plan schemes, as originally envisaged cannot be taken up fully, because the contemplated "Balance from Current Revenues" (BCRs) does not come through, Plan finances are diverted to non-Plan items, and time overruns increase costs. As a result, many schemes remain half done. While contributing little to output and to non-tax revenues, appointments have already been made, and capital structure has been put in place requiring maintenance and other expenditures. While old assets degenerate fast due to inadequate maintenance, new assets are not ready to contribute to output, the schemes remaining incomplete, thus causing a double blow to the productivity of government expenditures.

Apart from the Plan and non-Plan, albeit the Finance Commission vis-à-vis the Planning Commission dichotomy, there are other channels through which resource transfers that take place between the centre and the states providing room for much adhocism. This includes resource transfers through central Plan schemes administered by states and centrally sponsored schemes. There are also departmental transfers like DRDA schemes and Sarva Shiksha Abhiyan, which by-passes the state budgets.

2.5 Summary

The Finance Commission recommends devolution of funds to the states under two modes of transfers: (a) share in central taxes and (b) grants under Article 275 of the Constitution. The approach of the Finance Commissions in both cases have evolved over time taking into consideration some important constitutional amendments. To a large extent, the approach of the Finance Commission has been affected by the way the terms of reference to the Commission have been drafted.

Two important constitutional amendments during the period covered by the Eighth to the Twelfth Finance Commission are the 80th and 88th Amendments to the Constitution. The 80th Amendment relates to the alternative scheme of devolution
recommended by the Tenth Finance Commission. Although the central government had accepted to implement the alternative scheme with effect from the beginning of the award period of the Tenth Finance Commission, the actual amendment was carried out only in 2000.

The 80th Amendment provided for the sharing of all central taxes with the states except for Articles 268 and 269, taxes and earmarked cesses and surcharges. With this global sharing arrangement, under the provision of Article 270 the Finance Commissions have been able to develop a common set of criteria for all central taxes and follow an approach to the devolution of funds consistently some of the agreed principles of fiscal transfers in the literature. However, subsequent to the 80th Amendment, the central government has attempted to create additional fiscal space for itself by relying relatively more on cesses and surcharges and by placing the service tax under Article 268. Both of these are the exceptions to the provision of globalised sharing under Article 270.

In the case of grants, the approach of the Finance Commission is constrained by the way the terms of reference are cast. In particular, there is a reference to levels of tax and non-tax revenues reached in a base year. An elaborate set of terms of reference are prepared with mandatory clauses like the Commission 'shall' use a variety of considerations. There is also an asymmetry between the way in which needs of the central government are referred to vis-à-vis those of states.

The Finance Commissions themselves have followed an approach to determining grants-in-aid which contains adverse incentives as the approach is only partially normative and partially based on historical trends. This is not consistent with the first principles in the determination of grants as considered acceptably in the literature on the subject has also in the context of the principles uninitiated by the First Finance Commission itself. The problem is aggravated because of the dynamic linkages between the Finance Commission grants and plan assistance. Plan assistance is based partially on borrowing by the states. This gives rise to committed expenditures in the form of interest payments. In addition, a large part of plan assistance has been used for additional employment in the states giving rise to salary and pension liabilities. The Finance Commissions generally take these committed expenditures as given or as historically determined, thereby providing an incentive for the states to generate additional committed liabilities independent of its fiscal capacity or own revenue effort.
3

**Trends in Transfers:**  
**Pattern of Dependence**

In this Chapter, we look at the quantitative and qualitative dimensions of transfer and measure the degree of dependence of states on devolution of funds from the centre. For analyzing the impact of transfers on state finances, we look at their share in the combined revenue receipts before and after transfers. A comparison of these two profiles indicates the overall impact of transfers in so far as availability of resources to the two tiers of governments after transfers is concerned.

### 3.1 The Vertical Dimension

The vertical distribution of resources in India requires an overall view of all the current resources of the centre as well as the states. Since transfers from the centre take place through three channels, viz., Finance Commission, Planning Commission, and various central ministries, these need to be put together in order to see the extent of vertical transfers. Table 3.1 shows the composition of the combined revenue receipts of the centre and the states, and the share of the centre and states in these combined revenue receipts prior to transfers. In order to calculate the combined receipts, transfers from one tier to the other need to be netted out to avoid any double counting.

#### a. Relative Shares of Revenue Receipts before Transfers

Table 3.1 shows that states' own revenue receipts have varied over the years in the range of 34-41 per cent during the period 1984-85 to 2007-08. At its peak, in the nineties, states accounted for nearly 41 per cent of the combined revenue receipts. This contribution remained around an average of 38-39 per cent in the next 10 years. In the three years from 2005-06 to 2007-08, it has been on an average around 37 per cent. In other words, the pattern of vertical imbalance in raising revenues by the centre and the states has not changed by significant margins during the period covered by the Eighth to the Twelfth Finance Commissions. There is only some inter-year volatility.
### Table 3.1
Composition of Combined Revenue Receipts Prior to Transfers

(Rs. crore)

<table>
<thead>
<tr>
<th>Years</th>
<th>Central Revenue Receipts</th>
<th>State Revenue Receipts</th>
<th>Total Revenue Receipts</th>
<th>Share of States (per cent)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1984-85</td>
<td>27711</td>
<td>15313</td>
<td>43025</td>
<td>64.4 35.6</td>
</tr>
<tr>
<td>1985-86</td>
<td>33663</td>
<td>18092</td>
<td>51755</td>
<td>65.0 35.0</td>
</tr>
<tr>
<td>1986-87</td>
<td>38670</td>
<td>20581</td>
<td>59251</td>
<td>65.3 34.7</td>
</tr>
<tr>
<td>1987-88</td>
<td>43479</td>
<td>23798</td>
<td>67277</td>
<td>64.6 35.4</td>
</tr>
<tr>
<td>1988-89</td>
<td>50490</td>
<td>27328</td>
<td>77818</td>
<td>64.9 35.1</td>
</tr>
<tr>
<td>1989-90</td>
<td>60904</td>
<td>31654</td>
<td>92558</td>
<td>65.8 34.2</td>
</tr>
<tr>
<td>1990-91</td>
<td>64357</td>
<td>36329</td>
<td>100686</td>
<td>63.9 36.1</td>
</tr>
<tr>
<td>1991-92</td>
<td>76661</td>
<td>45782</td>
<td>122444</td>
<td>62.6 37.4</td>
</tr>
<tr>
<td>1992-93</td>
<td>86796</td>
<td>49519</td>
<td>136315</td>
<td>63.7 36.3</td>
</tr>
<tr>
<td>1993-94</td>
<td>88466</td>
<td>58347</td>
<td>146813</td>
<td>60.3 39.7</td>
</tr>
<tr>
<td>1994-95</td>
<td>104977</td>
<td>73021</td>
<td>177998</td>
<td>59.0 41.0</td>
</tr>
<tr>
<td>1995-96</td>
<td>126267</td>
<td>81971</td>
<td>208238</td>
<td>60.6 39.4</td>
</tr>
<tr>
<td>1996-97</td>
<td>147055</td>
<td>88238</td>
<td>235293</td>
<td>62.5 37.5</td>
</tr>
<tr>
<td>1997-98</td>
<td>159622</td>
<td>99486</td>
<td>259108</td>
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</tr>
<tr>
<td>1998-99</td>
<td>167344</td>
<td>108778</td>
<td>276122</td>
<td>60.6 39.4</td>
</tr>
<tr>
<td>1999-00</td>
<td>199309</td>
<td>125940</td>
<td>325249</td>
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<tr>
<td>2000-01</td>
<td>217816</td>
<td>138920</td>
<td>356736</td>
<td>61.1 38.9</td>
</tr>
<tr>
<td>2001-02</td>
<td>226758</td>
<td>152327</td>
<td>379085</td>
<td>59.8 40.2</td>
</tr>
<tr>
<td>2002-03</td>
<td>259094</td>
<td>169009</td>
<td>428103</td>
<td>60.5 39.5</td>
</tr>
<tr>
<td>2003-04</td>
<td>303508</td>
<td>192861</td>
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<td>61.1 38.9</td>
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<td>975368</td>
<td>63.4 36.6</td>
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</table>

Source (Basic Data): Ministry of Finance, Indian Public Finance, various years.
The Commission period-wise averages indicate that the share of centre in the combined revenue receipts came down from 65 per cent during the period of the Eighth Finance Commission to 61 per cent during the period of the Eleventh Finance Commission period and has since risen to about 63 per cent.

Table 3.2 shows the relative position of the centre and the states in the combined revenue receipts after transfers. The picture of relative contributions gets reversed in terms of the relative availability of resources. The share of states in the combined revenue receipts after transfers has been in the range of 58-69 per cent during the period 1984-85 to 2007-08. If inter-year variations are ignored, then on an average the share of the states in the combined revenue receipts shows only small variations since the average has remained between 61-64 per cent considering the broad range. In fact, the dependence of states on transfers was the highest during the first half of the nineties and since then it may have come down by about one percentage point.

The Commission period-wise averages indicate that the share of states in the combined revenue receipts after transfers increased from 61.6 per cent during the Eighth Finance Commission period to 64.7 per cent during the Ninth and then fell marginally to a little above 63 per cent. While the centre's share came down from 38.4 per cent during the Eight Finance Commission to 35.3 per cent during the Ninth and thereafter remained around 37 per cent.

### 3.2 Composition of Transfers

Table 3.3 shows the composition of transfers consisting of states' share in central taxes and total grants. This composition also shows variations only in a narrow range. The averages covered by the different Finance Commissions indicate that the share of central taxes accounted for about 51-60 per cent of the total transfers. Correspondingly grants (Finance Commission grants as well as other grants) contributed about 36-48 per cent of total transfers. In terms of the composition of transfers, the share of tax devolution was as high as 60.6 during the period covered by the Tenth Finance Commission but for Eighth, Ninth and Twelfth Finance Commissions, it was marginally above 54 per cent.

### 3.3 Annual Buoyancies of Central and State Taxes

Buoyancy of a tax is defined as percentage change in tax revenue relative to percentage
Table 3.2
Central and State Revenue Receipts After Transfers

<table>
<thead>
<tr>
<th>Years</th>
<th>Central Revenue Receipts</th>
<th>State Revenue Receipts</th>
<th>Total Revenue Receipts</th>
<th>Share of Centre (per cent)</th>
<th>Share of States (per cent)</th>
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<td>63.6</td>
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Averages
1984-89   38.4                        61.6
1989-95   35.3                        64.7
1995-00   37.1                        62.9
2001-05   36.9                        63.1
2005-08   36.5                        63.5

Source (Basic Data): Ministry of Finance, Indian Public Finance, various years.
### Table 3.3
Composition of Transfers (per cent)

<table>
<thead>
<tr>
<th>Year</th>
<th>States’ Share in Central Taxes</th>
<th>Statutory Grants</th>
<th>Other Grants</th>
<th>Total Grants</th>
<th>Total Transfers</th>
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</table>

**Source (Basic Data):** Ministry of Finance, Indian Public Finance, various years.

change in tax base. Considering GDP at market prices as indicative of tax base for the aggregate tax revenues, we consider the annual buoyancy of gross central tax revenues as well as the state tax revenues. Table 3.4 shows the respective buoyancies for the periods of the Eighth to the Twelfth Finance Commissions. It will be seen that in general
### Table 3.4
Annual Buoyancies of Central and State Taxes

<table>
<thead>
<tr>
<th>Years</th>
<th>Total Tax Revenue</th>
<th>Buoyancies of Cross Central Tax Revenues</th>
<th>States Own Tax Revenue</th>
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<td>1.221</td>
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**Source (Basic Data):** Indian Public Finance Statistics and NAS.

the centre's tax buoyancy is higher than that of the states. However, since the shares of the states in tax devolution were increased marginally in normal terms, the dependence of the states on central transfers has remained stable. In the case of the Tenth Finance Commission the share of the states was put at 29 per cent and in the case of the Twelfth Finance Commission it was increased to 30.5 per cent.
Table 3.5

Dependence of States on Central Taxes

<table>
<thead>
<tr>
<th>Finance Commissions</th>
<th>Years</th>
<th>Share in Central Taxes as % of States’ Revenue Receipts</th>
<th>Share of Central Taxes in Gross Central Tax Revenues</th>
<th>Gross Central Tax Revenue as % of GDPmp</th>
<th>States’ Revenue Receipts as % of GDPmp</th>
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</tbody>
</table>

Commission Period Averages

<table>
<thead>
<tr>
<th>Finance Commissions</th>
<th>Share in Central Taxes as % of States’ Revenue Receipts</th>
<th>Share of Central Taxes in Gross Central Tax Revenues</th>
<th>Gross Central Tax Revenue as % of GDPmp</th>
<th>States’ Revenue Receipts as % of GDPmp</th>
</tr>
</thead>
<tbody>
<tr>
<td>Eighth</td>
<td>22.83</td>
<td>25.20</td>
<td>10.21</td>
<td>11.26</td>
</tr>
<tr>
<td>Ninth</td>
<td>22.74</td>
<td>26.70</td>
<td>9.79</td>
<td>11.47</td>
</tr>
<tr>
<td>Tenth</td>
<td>23.52</td>
<td>27.59</td>
<td>8.97</td>
<td>10.53</td>
</tr>
<tr>
<td>Eleventh</td>
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<td>27.00</td>
<td>8.98</td>
<td>10.97</td>
</tr>
<tr>
<td>Twelfth</td>
<td>22.77</td>
<td>26.19</td>
<td>11.04</td>
<td>12.69</td>
</tr>
</tbody>
</table>

Source (Basic Data): Ministry of Finance, Indian Public Finance, various years.
3.4 Dependence of States on Central Transfers

a. All States

We measure dependence of states on devolution of funds from the centre by the relative share of such devolution in state's total revenue receipts. This has been done for the devolution on central taxes and for total devolution of funds. Table 3.5 shows the dependence of states in the central taxes. States' share in the central taxes have been in the range of 22 to 23 per cent of the states' gross revenue receipts indicating that the dependence of the states on central tax devolution has not gone up. There is, however, some increase in the states' share in central taxes as percentage of centre's gross tax revenues, which has gone up from an average of about 25 per cent in the Eighth Finance Commission period to about 26 per cent in the Twelfth Finance Commission period.

Table 3.6 shows the share of total transfer of funds received by the state governments as percentage of their total revenue receipts including the transfers. It also shows the contribution of the different components of these transfers viz., share in central taxes and grants. Considering averages over the Finance Commission periods, the broad pattern indicates relative stability in the profile of dependence of the states on devolution of funds from the centre. Total transfers as percentage of states revenue receipts came down marginally from a level of 43 per cent for the Eighth Finance Commission period to about 38.6 per cent for the Eleventh Finance Commission period but since then this share has gone up to 42 per cent. Within the overall transfers, the share of central taxes has remained remarkably stable as percentage of states revenue receipts being in the range of 22-23 per cent over the period covered by these five Finance Commissions. In fact, the share of statutory grants has gone up marginally whereas that of other grants has gone down marginally.

b. Individual States

As discussed above, considering states as a whole, there is no evidence of increased dependence of the states in the devolution from the centre. However, the pattern of dependence differs from state to state. There are some states where the dependence is extremely large. At the same time there are other states where the dependence is very limited. For the purpose of this analysis, we have divided the states into five groups. The general category states are divided into three groups, viz., high income states (Goa,
### Table 3.6

**Transfers as Percentage of States’ Revenue Receipts**

<table>
<thead>
<tr>
<th>Finance Commission</th>
<th>States’ Share in Central Taxes (per cent)</th>
<th>Statutory Grants (per cent)</th>
<th>Other Grants (per cent)</th>
<th>Total Grants (per cent)</th>
<th>Total Transfers (per cent)</th>
</tr>
</thead>
<tbody>
<tr>
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<td>2.06</td>
<td>17.21</td>
<td>19.27</td>
<td>41.31</td>
</tr>
<tr>
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<td>3.35</td>
<td>17.19</td>
<td>20.54</td>
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<td>16.89</td>
<td>19.57</td>
<td>43.12</td>
</tr>
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<td>17.43</td>
<td>20.49</td>
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<td>17.48</td>
<td>20.32</td>
<td>42.65</td>
</tr>
<tr>
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<td>2.99</td>
<td>13.09</td>
<td>16.08</td>
<td>40.89</td>
</tr>
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<td>5.41</td>
<td>14.33</td>
<td>19.73</td>
<td>42.90</td>
</tr>
<tr>
<td>1991-92</td>
<td>22.06</td>
<td>4.42</td>
<td>15.24</td>
<td>19.66</td>
<td>41.72</td>
</tr>
<tr>
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<td>15.83</td>
<td>20.25</td>
<td>43.81</td>
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<td>16.86</td>
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<td>42.63</td>
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<tr>
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<td>15.65</td>
<td>17.09</td>
<td>38.11</td>
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<tr>
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<td>4.01</td>
<td>11.73</td>
<td>15.74</td>
<td>37.97</td>
</tr>
<tr>
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<td>3.64</td>
<td>12.28</td>
<td>15.92</td>
<td>40.51</td>
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<tr>
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<td>1.88</td>
<td>13.39</td>
<td>15.27</td>
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<td>16.88</td>
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<tr>
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<td>12.09</td>
<td>17.28</td>
<td>38.77</td>
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<td>38.15</td>
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<td>14.11</td>
<td>19.48</td>
<td>42.20</td>
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<tr>
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<td>4.91</td>
<td>14.67</td>
<td>19.58</td>
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</table>

**Commission Period Averages**

<table>
<thead>
<tr>
<th></th>
<th>States’ Share in Central Taxes (per cent)</th>
<th>Statutory Grants (per cent)</th>
<th>Other Grants (per cent)</th>
<th>Total Grants (per cent)</th>
<th>Total Transfers (per cent)</th>
</tr>
</thead>
<tbody>
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<td>42.87</td>
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<td>3.77</td>
<td>15.16</td>
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<td>41.68</td>
</tr>
<tr>
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<td>12.60</td>
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<td>38.80</td>
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<tr>
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<td>5.36</td>
<td>13.61</td>
<td>18.96</td>
<td>41.73</td>
</tr>
</tbody>
</table>

**Source (Basic Data):** Ministry of Finance, Indian Public Finance, various years.
Gujarat, Haryana, Maharashtra and Punjab), middle income states (Andhra Pradesh, Karnataka, Kerala, Tamil Nadu, West Bengal and Chhattisgarh) and low income states (Bihar, Madhya Pradesh, Orissa, Rajasthan, Uttar Pradesh and Jharkhand). The special category states are divided into two groups. Group 1 consists of relatively high income states among the special category states. This group includes Himachal Pradesh, Jammu and Kashmir, Meghalaya, Sikkim and Uttaranchal. Group 2 includes Arunachal Pradesh, Assam, Manipur, Mizoram, Nagaland and Tripura.

Table 3.7 indicates the pattern of change in dependence of these states considered as averages over the periods covered by Ninth to Twelfth Finance Commissions. Comparing first the general category states, the high income states are the least dependant and the low income states are the most dependent on Finance Commission transfers. This is only to be expected in a system where the fiscal transfer system attempts to bring about a degree of equalization in fiscal capacities of states with a view to addressing the horizontal imbalance problem.

We also consider changes in the pattern of dependence for individual states with respect to the total funds that they receive from the central government. Table 3.7 shows the share of transfers in the revenue receipts of the concerned states. In so far as the middle income states are concerned, apart from West Bengal and Kerala, there is some evidence of reduction in the pattern of dependence. In the case of low income states, the degree of dependence of Bihar and Madhya Pradesh seems to have clearly increased but there are no signs of such increases in the case of Orissa, Rajasthan, and Uttar Pradesh. Among the special category states there are no noticeable cases of increased dependence during the period covered by the four Commissions. As such, apart from a few cases, where there is evidence of increase in the degree of dependence of the states on central transfers, the pattern of dependence seems more or less stable.

Thus, considering both the vertical and horizontal dimensions of transfers, there is no evidence that shows that the dependence of states on central transfers has increased. Only a very limited number of states such as Bihar show a very clear increase in dependence on transfers. The issue relates more to the qualitative aspects of transfers. There are a few noticeable patterns in respect of these qualitative aspects:

First, the centre has relied progressively more on cesses and surcharges in recent years, which are kept outside the purview of transfers by the Finance Commissions. Even if part of these is shared with the states, such sharing is more ad hoc and non-transparent.
### Table 3.7

**Total Transfers from the Centre as Percentage of Revenue Receipts of the States**

(Per cent)

<table>
<thead>
<tr>
<th>Period</th>
<th>Goa</th>
<th>Gujarat</th>
<th>Haryana</th>
<th>Maharashtra</th>
<th>Punjab</th>
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</thead>
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<td>15.91</td>
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<tr>
<td>1995-00</td>
<td>15.03</td>
<td>19.91</td>
<td>14.73</td>
<td>16.24</td>
<td>15.63</td>
</tr>
<tr>
<td>2005-08</td>
<td>15.72</td>
<td>25.01</td>
<td>15.66</td>
<td>22.39</td>
<td>21.57</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Andhra Pradesh</th>
<th>Karnataka</th>
<th>Kerala</th>
<th>Tamil Nadu</th>
<th>West Bengal</th>
<th>Chhattisgarh</th>
</tr>
</thead>
<tbody>
<tr>
<td>1990-95</td>
<td>36.03</td>
<td>27.10</td>
<td>33.37</td>
<td>30.30</td>
<td>43.36</td>
</tr>
<tr>
<td>1995-00</td>
<td>36.53</td>
<td>26.04</td>
<td>28.11</td>
<td>25.46</td>
<td>43.40</td>
</tr>
<tr>
<td>2000-05</td>
<td>31.25</td>
<td>26.35</td>
<td>26.20</td>
<td>22.59</td>
<td>46.21</td>
</tr>
<tr>
<td>2005-08</td>
<td>31.22</td>
<td>27.21</td>
<td>30.53</td>
<td>23.73</td>
<td>50.12</td>
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</table>

<table>
<thead>
<tr>
<th>Bihar</th>
<th>Madhya Pradesh</th>
<th>Orissa</th>
<th>Rajasthan</th>
<th>Uttar Pradesh</th>
<th>Jharkhand</th>
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</thead>
<tbody>
<tr>
<td>1990-95</td>
<td>59.47</td>
<td>41.79</td>
<td>59.80</td>
<td>43.99</td>
<td>52.21</td>
</tr>
<tr>
<td>1995-00</td>
<td>60.72</td>
<td>39.26</td>
<td>56.79</td>
<td>38.42</td>
<td>49.29</td>
</tr>
<tr>
<td>2000-05</td>
<td>72.19</td>
<td>42.34</td>
<td>55.00</td>
<td>40.98</td>
<td>49.70</td>
</tr>
<tr>
<td>2005-08</td>
<td>78.73</td>
<td>48.07</td>
<td>56.14</td>
<td>41.82</td>
<td>51.85</td>
</tr>
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</table>

<table>
<thead>
<tr>
<th>Himachal Pradesh</th>
<th>J&amp;K</th>
<th>Meghalaya</th>
<th>Sikkim</th>
<th>Uttarakhand</th>
</tr>
</thead>
<tbody>
<tr>
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<td>71.92</td>
<td>83.36</td>
<td>84.14</td>
<td>70.40</td>
</tr>
<tr>
<td>1995-00</td>
<td>66.97</td>
<td>84.33</td>
<td>82.40</td>
<td>28.03</td>
</tr>
<tr>
<td>2000-05</td>
<td>67.80</td>
<td>79.77</td>
<td>79.79</td>
<td>43.39</td>
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<tr>
<td>2005-08</td>
<td>64.81</td>
<td>81.14</td>
<td>46.07</td>
<td>57.42</td>
</tr>
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</table>

<table>
<thead>
<tr>
<th>Arunachal Pradesh</th>
<th>Assam</th>
<th>Manipur</th>
<th>Mizoram</th>
<th>Nagaland</th>
<th>Tripura</th>
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<td>1990-95</td>
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<td>64.98</td>
<td>91.25</td>
<td>90.55</td>
<td>92.10</td>
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</table>

**Source (Basic Data):** Reserve Bank of India, State Finances: A Study of Budgets, various years.
Second, the centre has continued to make decisions unilaterally where there is bound to have serious impact on the state finances. The impact of salary revisions of the centre is largely transmitted to the states. These are only of expenditure side 'vertical externality' and require a joint mechanism for arriving at decisions. Third, the TOR of Finance Commissions are unilaterally decided by the centre even though the states are equally important players in the federal fiscal structure. Fourth, the way the centre has handled intermediation of debt to the states, has led to a distorted pattern of expenditure. These are further discussed below.

3.5 Fiscal Relations between Centre and States: Selected Issues

a. Cesses and Surcharges Levied by the Central Government

The central government has been levying a number of cesses and surcharges on both direct and indirect taxes. These are kept out of the purview of sharing with the states under the recommendations of the Finance Commissions as provided in the 80th Constitutional Amendment. Even if these are shared with the states, the methodology of the sharing or allocation among states is determined at the discretion of the concerned department(s). Some of the main cesses and surcharges for the main central taxes are mentioned below:

1. Customs
   (i) In case of customs there is a cess on motor spirit leviable by the Finance Act (2) of 1998.
   (ii) There is also a cess on high speed diesel oil leviable by the Finance Act of 1999. In addition there is a surcharge on motor spirit leviable by the Finance Act of 2002.
   (iii) In addition there is education cess levied at 2 per cent on aggregate duties of customs.
   (iv) Further there is secondary and higher education cess levied at 1 per cent on aggregate duties of customs.

2. Union Excise Duties
   (i) Education cess is leviable at 2 per cent on the aggregate duties of excise.
   (ii) Secondary and higher education cess is levied at 1 per cent on the aggregate duties of excises.
(iii) Cess on motor spirit is levied under the Finance Act of 1988.
(iv) Cess on high speed diesel is levied under the Finance Act of 1999.
(v) Surcharge on motor spirit is levied by the Finance Act of 2002.
(vi) Surcharge on pan masala and tobacco products is levied as an additional duty of excise from the budget of 2005-06.

Table 3.8
Cesses and Surcharges raised by the Central Government

<table>
<thead>
<tr>
<th>Year</th>
<th>Education Cess</th>
<th>Higher Education Cess</th>
<th>Direct Tax Surcharge*</th>
<th>Cess on Crude</th>
<th>Cesses on Commodities (UED)</th>
<th>Surcharge on Motor Spirit (UED)</th>
<th>Surcharge on Pan Masala (UED)</th>
<th>Cesses on Exports</th>
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</thead>
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Source (Basic Data): Union Finance Accounts, various years and Central Budget 2007-08 and 2008-09.  
# Excludes surcharge on sales tax; UED: union excise duties.
3. Service Tax
   (i) Education cess is levied at the rate of 2 per cent.
   (ii) Secondary and higher education cess is levied at the rate of 1 per cent.

**Table 3.9**

Cesses and Surcharges as Percentage of Centre's Gross Tax Revenues

(Rs. crore)

<table>
<thead>
<tr>
<th>Year</th>
<th>Cesses and Surcharges</th>
<th>Centre's Gross Tax Revenues</th>
<th>Cesses and Surcharges as % of Centre's Gross Tax Revenues</th>
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<tbody>
<tr>
<td></td>
<td>Cesses</td>
<td>Surcharges</td>
<td>Total</td>
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<td>2001-05</td>
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Source (Basic Data): Union Finance Accounts, various years and Central Budget 2007-08 and 2008-09.
4. Corporation Tax
   (ii) Education Cess is levied at the rate of 2 per cent.
   (iii) A surcharge is also levied.

5. Income Tax
   (i) Education Cess is levied at the rate of 2 per cent.
   (ii) A surcharge is also levied.

Table 3.8 shows amounts raised under various cesses and surcharges. In recent years education cess and higher education cess taken together contribute nearly Rs. 20,000 crore, in addition the direct tax surcharges also are estimated to contribute about Rs. 28,000 crore in 2008-09. On the side of indirect taxes the cesses on crude oil and surcharge on motor spirit contribute another Rs. 20,000 crore.

Table 3.9 shows cesses and surcharges as percentage of centre's gross revenues. These are now contributing nearly 12 per cent of centre's gross revenue receipts. Although in the 80th Amendment to the Constitution cesses and surcharges where kept out of the purview of Article 270, this exception was made only to accommodate centre's need for resources in extraordinary situations. Particularly, surcharges are not meant to serve as a vehicle to avoid sharing certain portions of tax revenue with the states on a continuing basis.

b. Vertical Externality of Expenditure

There are some areas in which decisions taken by the central government have an externality impact on the state governments. These impacts may be quite substantial. One significant example is the impact of salary revisions undertaken by the central government following recommendations of the Central Pay Commissions. Both Fifth and Sixth Pay Commissions are clear examples of this externality impact on state government expenditures. Once the central government decides on a certain structure of pay scales for its employees, it is very difficult for the state governments to resist a similar increase. State governments have to undertake such increases, irrespective of their own fiscal capacities or the history of recruitment which may have led to a much higher size of government employees relative to their population. In federal system such vertical externalities are inevitable. This also applies to pensions. In cases where strong vertical externalities are present whether on the revenue or expenditure side, the
central government needs to take decisions after joint consultation with the state governments.

a. Finance Commission: Terms of Reference

Another critical qualitative dimension of the relations between the centre and the state is the finalization of terms of reference of the Finance Commission. The core tasks of the Finance Commissions have already been defined in the constitution. But the central government has got into the habit of not only addressing additional tasks to the Finance Commission but also laying out an elaborate set of guidelines for the Finance Commission for making their recommendations. In this process, states are not consulted in a manner that would suitably reflect their views.

These paras referred to the Finance Commissions made reference to mandatory ‘considerations’, as the Commissions were asked by the President that in making its recommendations, the Commission “shall” have regard to the considerations stated in the sub-clauses, among others. The use of the words, the Commission “shall” imparts this clause a ‘directive’ character. This appears to violate the provision and spirit of Article 280(4), and of the Finance Commission (Miscellaneous Provisions) Act of 1951 as amended in 1955, whereby the Commission is to determine their own procedure. Article 280(4) clearly provides that “the Commission shall determine their procedure”. Since the central government is itself an interested party, it has started submitting a memorandum to the Finance Commission (beginning with the Tenth Finance Commission) to make its views known rather than issue guidelines or give directives through the TOR. The duties of a Finance Commission are specified in the Constitution itself the TOR should simply enumerate the matters on which the recommendations of a Finance Commission are sought, leaving the Commission free to determine the scope of their recommendations and the methodology on which these are to be based.

The phrase “shall have regard”, appeared for the first time in the TOR of the Fifth Finance Commission in the context of resources and needs of the central government in Para 5 of their TOR, which read: “the Commission in making its recommendations on the various matters aforesaid shall have regard to the resources of the central government and the demands thereon on account of the expenditure on civil administration, defence, and border security, debt servicing and other committed expenditures or liabilities”. This
clause was repeated in the TOR of the Sixth Finance Commission. The practice of having a para containing several ‘considerations’ started with the Seventh Finance Commission where, for the first time, the phrase “in making its recommendations, the Commission shall have regard, among other considerations, to …” was used. This para containing “considerations” has, since then been part of the TOR of all successive Finance Commissions. However, in the case of the Ninth Finance Commission, the TOR were converted fully into a directive by using the phrase in Para 4 of its TOR: “In making its recommendations, the Commission shall …”. The tasks were enlisted but these were not mere considerations. The Chief Minister of Kerala had written to the Chairman of the Ninth Finance Commission articulating misgivings and apprehensions about the use of the word ‘shall’ in Para 4 of the Presidential Notification which appeared to be “mandatory almost amounting to a directive” (Para 1.7 of the First Report of the Ninth Finance Commission). Also, the suggestion to take account of all the committed liabilities in the case of the Centre and the absence of a similar suggestion for the States gave rise to misgivings that the ‘guidelines’ were loaded in favour of the Centre. Similar apprehensions were expressed by a number of participants in a seminar on Issues before the Ninth Finance Commission. To dispel these, the Chairman of the Commission wrote to all the Chief Ministers (Para 1.7 of their First Report) setting out the Commission’s perception of their role and obligations. He mentioned that it was the “Commission’s prerogative” to adopt such approach and method as it considered fit and appropriate on subjects covered by (a) and (b) of Article 280(3) of the Constitution.

The phrase “The Commission shall have regard, among other considerations to …” was reintroduced in the TOR of the Tenth Finance Commission and this practice has been continued since. A study of the sub-clauses of this para for the Tenth, Eleventh, and Twelfth Finance Commissions indicates that this has been utilised to refer to the following areas:

(i) Resources and needs of the Centre;

(ii) Resources and needs of the States, particularly the consideration of the entire revenue account vis-à-vis only the non-plan revenue account;

(iii) Methodology to be followed by the Commission in determining transfers including choice of the base year;

(iv) Maintenance and upkeep of capital assets and maintenance in respect of plan schemes completed by a specified date;
(v) Up-gradation of standards of services in general administration and non-
developmental sectors;

(vi) Returns on government investments in specified sectors including irrigation
and power projects; and

(vii) Fiscal management and economy in expenditure consistent with efficiency.

From the Eighth Finance Commissions onwards, the para mandating the use of the
1971 population was also introduced. This para provides that “in making its
recommendation on various matters, the Commission will take the base of population
figures as of 1971, in all such cases where population is a factor for determination of
devolution of taxes and duties and grants-in-aid. Such a direction has been given to all
Finance Commissions since the Seventh. Commission The only change in the case
of the TOR of the Twelfth Finance Commission was the substitution of the phrase
“will take the base of population figures as of 1971” in place of “shall adopt the
population figures of 1971”. Although population figures are available for 1981, 1991
and 2001 from the relevant Census exercises, the Finance Commissions have been
asked not to use these in matters relating to devolution.

It may be noted that following the ‘Family Welfare Programme: A Statement of Policy’
resolution to adopt the 1971 population, the Constitution has been amended for
limiting the number of members to the Lok Sabha and to the ‘State Legislative
Assemblies’. No specific amendment has been made in respect of Centre-State financial
relations.

Some relevant considerations in this context are:

(i) A direction like this is not consistent with Article 280(4) and the Finance
Commission’s (Miscellaneous Provisions) Act, 1951 as amended in 1955
whereby the Commission is to determine their own procedure;

(ii) If the idea is to ‘penalize’ states for not effectively controlling population growth,
this should apply only to unsatisfactory performance in controlling the birth rate.
States should not be penalized for better performance in reducing death rates or in-
migration of population. The method of providing the right incentives with
appropriate indicators should have been left to the Finance Commission;

(iii) There is no constitutional sanction for this. The provisions regarding the use of
1971 population relate to election and reservation matters (e.g., Article 330). There is no relationship between considerations for determining the number of seats for representation of population and determination of financial assistance to States for providing services to the entire population residing in their respective jurisdictions. In Articles 243(f) and 243 (g), referring respectively to the panchayats and municipalities the term ‘population’ has been defined as follows: “population’ means the population as ascertained at the last preceding census of which the relevant figures have been published”.

d. Service Tax

The structure of the Indian economy has been moving progressively towards the services sector. The service tax is going to grow further in importance. In such a context, placing the service tax as part of Article 268 and thereby taking it out of the purview of Article 270, which provides for the sharing of the central taxes with the states is also qualitatively not conducive to a healthy status of centre-state relations even though in practice at the moment the same share in service tax revenue as for other central taxes is being provided.

The provision of Article 268A is as follows:

“268A. Service tax levied by Union and collected and appropriated by the Union and the States.

(1) Taxes on services shall be levied by the Government of India and such tax shall be collected and appropriated by the Government of India and the States in the manner provided in clause (2).

(2) The proceeds in any financial year of any such tax levied in accordance with the provisions of clause (1) shall be- (a) collected by the Government of India and the States; (b) appropriated by the Government of India and the States, - in accordance with such principles of collection and appropriation as may be formulated.”

The Seventh Schedule of the Constitution has also been accordingly amended by placing the tax on services as Entry 92B in the Union List.

In this context, the Twelfth Finance Commission has observed as follows: ‘…any legislation that is enacted in respect of service tax must ensure that the revenue accruing to a state under the legislation should not be less than the share that would accrue to it, had the
entire service tax proceeds been part of the shareable pool’ (Para 7.22, Report of the Twelfth Finance Commission)

e. Centre's Intermediation of State Debt and Structure of State Expenditure

The central government has been intermediating in the process of raising state debt until the Twelfth Finance Commission recommended that such intermediation may be discontinued except for on-lending of external assistance and small savings. Centre's intermediation of states debt and periodic relief relating to debt servicing by successive Finance Commissions have lead to considerable adverse incentives in the system. Many states have incurred unsustainable levels of debt and this has impacted on the structure of expenditure. In particular, the level of primary expenditure (expenditures excluding interest payments) relative to state GSDPs has gone down in the nineties. With primary expenditures, the share of capital expenditure has also gone down for several states because of the pre-emptive demand of growing interest payments while revenue receipts had remained more or less stable relative to GSDP.

The structure of expenditure of the states, considered together, has changed in a manner that the share of interest payments has progressively increased from the period covered by the Eighth Finance Commission when it was in the range of 7 to 10 per cent of the total expenditure to a peak of 16-19 per cent during the period covered by the Eleventh Finance Commission (Table 3.10). The share of pensions also increased over these years from a little less than 3 per cent of total expenditure to a peak of about 7-8 per cent during the period covered by the Eleventh Finance Commission. This change in favour of the committed expenditure was at the cost of revenue expenditure other than interest payments and pensions (non-pension primary revenue expenditures) as also capital expenditures. The share of capital expenditure in total expenditure was about 21 per cent in 1984-85. It fell to about 11-14 per cent in the mid- to late-nineties. Since then it has picked up again. The non-pension primary revenue expenditures have fallen from the range of more than 68-70 per cent in the mid-eighties to less than 60 per cent in more recent years.

These changes cannot be said to directly follow from the recommendations of the Finance Commission. But it does have some link to the adverse incentives of coming from partial gap-filling and encouragement of borrowing both by the plan process and periodic debt-relief given by successive Finance Commissions.
Table 3.10
States: Structure of Expenditure (Per cent to Total Expenditure)

<table>
<thead>
<tr>
<th>Year</th>
<th>Interest Payments</th>
<th>Pension and Retirement Benefits</th>
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<th>Capital Expenditure</th>
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<td>18.83</td>
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</table>

Source (Basic Data): Indian Public Finance Statistics (various issues).

In the past, the Finance Commissions have by and large taken interest payments of the base year as actual and justified committed liabilities. This leaves considerable adverse incentives in the system as states can finance current expenditures by additional borrowings and create liabilities to be underwritten by future Finance Commissions. Among federations
that use a normative determination of debt charges, i.e., interest payments, an important example is that of Australia.

Following the recommendation of the Twelfth Finance Commissions, centre's intermediation in states' borrowing has been discontinued. The reliance is now far more on market-based discipline. For a market based discipline to work, it is required that a hard budget constraint is imposed on the states. This would imply that the cost of borrowing will be determined on the basis of the fiscal viability and risk assessment specific to that state. A fiscally weak state would have to pay a higher risk premium for its borrowing from the market. These signals are currently muted because states, weak or strong, often pay the same interest rates on various instruments. Interest rates may therefore sharply rise for a state which is fiscally slipping, alerting at once about the developing fiscal weakness of the state. The market would normally evaluate the states on the basis of credit ratings which various credit rating agencies may develop using a variety of criteria.

3.5 Summary

In this Chapter, we have examined the pattern of dependence of the states on devolution of funds from the centre over the period covered by recommendations of the Eighth to the Twelfth Finance Commissions for which data are available i.e., from 1984-85 to the budget estimates of 2007-08. The following are the main findings:

(i) The share of the states in the combined revenue receipts of the centre and the state governments net of inter-governmental flows, prior to transfers, shows that there has been an increase in the share of states from 35 per cent during 1984-89 to 39 per cent during 2001-05. After that it has fallen by about 2 percentage points.

(ii) The share of states in the combined revenue receipts after transfers show that the relative availability of funds gets reversed as compared to the relative pattern before transfers. In particular, the share of the centre, which was more than 60 per cent of the combined revenue receipts before transfers, becomes about 35-38 per cent after transfers. In general, there is relative stability in the share of the centre and states in the combined revenue receipts after transfers.

(iii) The composition of transfers as between states share in central taxes and grants (covering both Finance Commission grants and other grants) also indicates a
pattern which is by and large stable. States' share in central taxes has been on average about 56 per cent with some variations and correspondingly the share of grants has been about 44 per cent.

(iv) The dependence of the states on central taxes is measured by the ratio of states' share in central taxes as percentage of states revenue receipts. The average for the period covered by respective Finance Commissions from the Eighth Commission onwards indicates that this ratio was about 22 per cent or just above for Eighth, Ninth, Eleventh and Twelfth Finance Commission periods. In the case of Tenth Commission, it was about 23.5 per cent. We may note that share of states in central taxes as percentage of gross central revenues has also been stable in the range of 25-27 per cent. This share however is still less than the benchmark of 29 per cent, which was recommended by the Tenth Finance Commission while outlining the alternative scheme of devolution.

(v) Considering dependence of the states more comprehensively, we measure total transfers (share in taxes plus all grants) as percentage of states revenue receipts. Total transfers as percentage of states' revenue receipts account for nearly 41 per cent, and this pattern has also remained stable.

(vi) Considering individual states the pattern of dependence indicates that apart from a very limited number of states such as Bihar and to some extent West Bengal there is no evidence of increased dependence of the states on devolution of funds from the centre.

This study of pattern of dependence indicates that the fiscal relations between the centre and the states are affected more by qualitative dimensions of fiscal relations rather than quantitative dimensions. In particular, the following aspects are notable:

(a) The central government has relied to a considerable extent on additional cesses and surcharges in particularly in recent years. Even though part of the cesses may be allocated to the states, such allocation mechanisms trend to be non-transparent and discretionary.

(b) Even in the case of plan grants there is less reliance on the Gadgil formula and a larger portion is being allocated in an ad hoc way.

(c) Placement of the service tax under Article 268A rather than Article 270 is also not conducive to maintenance of healthy fiscal relations between the
centre and the states even though at present the same share of service tax is being given to the states as for other central taxes.

(d) The approach of the Finance Commission is also affected by the way the terms of reference are cast. In particular, Finance Commission is mandated to use some specific year as base year. In addition, they have to provide for considerable liabilities due to the mechanism of plan assistance which has a limited time perspective and does not provide for the implications of the long-term liabilities created by the plan process on State finances.

(e) The composition of state expenditure has been affected such that the share of interest payments and other committed liabilities has increased and the share of capital expenditure has fallen. This is partly the result of the way in which revenue-gap grants are determined by the Finance Commission and borrowing is encouraged by the Planning Commission.
Conclusions: Reforming the System of Fiscal Transfers

4.1 Fiscal Relations: Quantitative and Qualitative Aspects

Fiscal transfers from the centre to the states take place through the Finance Commission, Planning Commission, and the central ministries. The overall system of fiscal transfers suffers from many inadequacies and deficiencies. This also affects the nature of fiscal relations between the centre and the states. In this study, we have reviewed the fiscal relations between the centre and the states, in terms of both its quantitative and qualitative aspects, focusing on the period covered by the Eighth to the Twelfth Finance Commission.

Fiscal relations can be considered to be healthy and efficient if the states maintain sufficient autonomy with regard to expenditures undertaken by them on items listed in the State List and there is no over-centralisation of the combined revenue or expenditure space. Wherever there are vertical externalities affecting the revenue and expenditure decisions of one tier of government by the other tier of government, fiscal relations are best served by processes of mutual consultations or joint decision making.

4.2 Finance Commissions: Sharing of Centre's Taxes

The Finance Commission recommends devolution of funds to the states under two modes of transfers: (a) share in central taxes and (b) grants under Article 275 of the Constitution. The approach of the Finance Commissions in both cases has evolved over time taking into consideration some important constitutional amendments. To a large extent, the approach of the Finance Commission has been affected by the way the terms of reference to the Commission have been drafted.

Two major amendments to the Constitution affecting the tax devolution process since the period of the Eighth Commission were the 80th and the 88th Amendments. The 80th Amendment brought all central taxes excluding Article 268 and 269 taxes under Article
270 for sharing with the states under recommendations of the Finance Commission. The 88th Amendment however placed the service tax outside of this generalized arrangement of sharing. In addition, the central government also began to rely relatively more on cesses and surcharges. These developments have not been consistent with the spirit of the 80th Amendment but the Finance Commission have periodically and marginally increased the share of the states thereby neutralizing the impact of keeping cesses and surcharges out of the divisible pool under Article 270. The central government has also helped by giving to the states the same share of the service tax revenue as applicable to other central taxes.

4.3  Finance Commissions: Determination of Grants

In relation to grants, there has been a debate regarding the scope of Article 275 and 282 and the links between grants given by the Finance Commission and the assistance given by the Planning Commission to the states. In the case of grants, the approach of the Finance Commission is constrained by the way the terms of reference are cast. In particular, there is a reference to levels of tax and non-tax revenues reached in a 'base' year. An elaborate set of terms of reference are prepared with mandatory clauses like the Commission 'shall' use a specified set of considerations. There is also an asymmetry between the way in which needs of the central government are referred to vis-à-vis those of the states.

The Finance Commissions themselves have followed an approach to determining grants-in-aid, which contains adverse incentives as the approach is only partially normative and partially based on historical trends. This is not consistent with the first principles for the determination of grants as considered acceptable in the literature on the subject. It is also not consistent with the principles enunciated by the First Finance Commission itself. The problem is aggravated because of the dynamic linkages between the Finance Commission grants and plan assistance. Plan assistance is based partially on borrowing by the states. This gives rise to committed expenditures in the form of interest payments. In addition, a large part of plan assistance has been used for additional employment in the states giving rise to salary and pension liabilities. The Finance Commissions generally take these committed expenditures as given or as historically determined, thereby providing an incentive for the states to generate additional committed liabilities independent of its fiscal capacity or own revenue effort.
4.4 State's Dependence on Devolution of Funds

We have examined the main trends in relation to the devolution of funds to the states from the centre over the period covered by recommendations of the Eighth to the Twelfth Finance Commissions for which data are available i.e., from 1984-85 to the budget estimates of 2007-08 RE. It is observed that the share of the states in the combined revenue receipts of the centre and the state governments net of inter governmental flows, prior to transfers, shows that there has been an increase in the share of states from 35 per cent during 1984-89 to 39 per cent during 2001-05. After that it has fallen by about 2 percentage points.

After transfers, the share of states in the combined revenue receipts shows that the relative availability of funds gets reversed as compared to the picture before transfers. In particular, the share of the centre which was more than 60 per cent of the combined revenue receipts before transfers becomes about 35-38 per cent after transfers. In general, there is relative stability in the share of the centre and states in the combined revenue receipts after transfers. The composition of transfers as between states share in central taxes and grants (covering both Finance Commission grants and other grants) also indicates a pattern, which is by and large stable. States share in central taxes has been on average about 56 per cent with some variations and correspondingly the share of grants has been about 44 per cent.

In regard to dependence of states on devolution of funds from the centre, the following features may be highlighted.

1. The dependence of the states on central taxes is measured by the ratio of states' share in central taxes as percentage of states revenue receipts. The average for the period covered by respective Finance Commissions from the Eighth Commission onwards indicates that this ratio was about 22 per cent or just above for the Eighth, Ninth, Eleventh and Twelfth Finance Commission periods. In the case of the Tenth Commission, it was about 23.5 per cent. We may note that share of states in central taxes as percentage of gross central revenues has also been stable in the range of 25-27 per cent. This share however is still less than the benchmark of 29 per cent, which was recommended by the Tenth Finance Commission while outlining the alternative scheme of devolution.

2. Considering dependence of the states more comprehensively, we measure total transfers (share in taxes plus all grants) as percentage of states revenue receipts.
State's share of transfers as percentage of state's revenue receipts is also stable in the range of 38.5 to 42.9 per cent with some inter-variations.

3. Considering individual states, the pattern of dependence indicates that, apart from a very limited number of states such as Bihar and to some extent West Bengal, there is no evidence of increased dependence of the states on devolution of funds from the centre.

4.5 Qualitative Dimensions of Fiscal Relations

This study of pattern of dependence indicates that the fiscal relations between the centre and the states are affected more by qualitative dimensions of fiscal relations rather than quantitative dimensions. In particular, the following aspects are notable:

a. The central government has relied to a considerable extent on additional cesses and surcharges, particularly in recent years. Even though part of the cesses may be allocated to the states, such allocation mechanisms tend to be non-transparent and discretionary.

b. Even in the case of plan grants there is less reliance on the Gadgil formula and a larger portion is being allocated in an ad hoc way.

c. Placement of service tax under Article 268A rather than Article 270 is also not conducive to maintenance of healthy fiscal relations between the centre and the states even though at present the same share of service tax is being given to the states as for other central taxes.

d. The approach of the Finance Commission is also affected by the way the terms of reference are cast. In particular, Finance Commission is mandated to use some specific year as base year. In addition, they have to provide for considerable liabilities due to the mechanism of plan assistance, which has a limited time perspective and does not provide for the implications of the long-term liabilities created by the plan process on State finances leading to problems of debt-sustainability.

4.6 Reforming System of Transfers: Some Suggestions

a. Use of Updated Information

In the literature on the subject of fiscal transfers, it is generally agreed that vertical
transfers should be broadly consistent with the imbalance between assigned responsibilities and resources. In the case of horizontal transfers, the system of transfers should be guided by equalization, which is consistent with equity as well as efficiency. This requires that a normative approach should be used to determine fiscal capacity and tax effort. To some extent, the exercise of using a normative approach is constrained by information lags. The data on population pertains to 1971 (mandated by the TOR). By the time the recommendation period of the Thirteenth Finance Commission is over, it will be out of date by more than 40 years. Even the data on GSDP, which serves as indicator of revenue base, will be dated by about 8 years by 2014-15. It is difficult to see the relevance of 1971 population census data when population of all states was about 54 crore, whereas 2001 census puts the all-India population at more than 100 crore. Even if the implicit objective is to penalize states, which have done less well in comparative terms in controlling population growth, the determination of the suitable incentives should be left to the Finance Commission.

b. Terms of Reference

There is no need for the central government to put forward extremely detailed TOR leaving the Finance Commission free to determine its approach with reference to provisions of Article 280. If the contemporary economic situation warrants a special reference, the TOR should be finalized after detailed consultations with the state governments.

c. Planning Commission Transfers

In the case of plan assistance, the proportion between grants and loans at 30:70 for the general category states and 10:90 for the special category states has a counterpart in the interest rate charged by the central government on the plan loans to the states. The Twelfth Finance Commission had recommended that grants and loans should be delinked and given on different sets of consideration. Grants should be given according to needs and loans according to capacity to borrow. Plan grants should be given as genuine grants and states may be encouraged to borrow from the market directly. The plan size of each state needs to take into account the sustainable level of debt and the capacity to borrow from the market. However, the Planning Commission has continued to insist on maintaining such a link even after the discontinuation of centre's intermediation of state loans.
We have also noted that the structure of expenditure of the states has changed in favour of non-developmental expenditures during the period under review. In particular, the share of interest payments and pensions has increased and the share of capital expenditure has fallen during this period. Part of the distortion in the structure of expenditure derives from the distinction between plan and non-plan expenditures. It is inefficient to show preference for creating new assets or undertaking new schemes being part of the plan, while sacrificing maintenance of already created assets. As a result, there remain many incomplete projects/schemes not yielding services on one side, and ill-maintained and fast depreciating assets, on the other. Over time, plans have become more scheme-oriented rather than project-oriented, so that assets that could provide returns to service the debt that was used to finance plan expenditures are neither being created nor maintained.

In the case of centrally sponsored schemes also there should only be the grant element and no loans linked to grant. A state should be given its total entitlement of grants and allowed to select its own mix of centrally sponsored schemes floated by different ministries, within the limit of the total grant. The centrally sponsored schemes would then start competing among themselves and pressure would come on the ministries to design schemes that are in demand. This would do away with the present supply driven approach where schemes are characterized by large numbers and other deficiencies. It would be much better if the Planning Commission adopts a planning based approach. Grants to the extent of 100 per cent may be given for projects dealing with poverty alleviation, health and education etc. where there is little scope of generating additional revenues as a result of additional expenditures. In the case of most economic projects dealing with areas like power, irrigation, transport etc. assistance may be given fully as loans because the states would be able to recover the cost of servicing the debt resulting from the loans.

d. Fiscal Responsibility Legislations

State finances in the recent years have been characterized by issues of debt-sustainability. Under the recommendations of the Twelfth Finance Commission, particularly following an comprehensive debt relief scheme, 26 out of 28 states have enacted fiscal responsibility legislations. In a few cases where there were existing fiscal responsibility legislations, certain modifications were introduced so as to provide for bringing their revenue accounts into balance and containing their fiscal deficits to a
level of 3 per cent of GSDP or less by 2008-09. Available data indicate that states, considered collectively, have achieved these objectives but the central government is most likely to miss-out on both objectives even though it had enacted its own fiscal responsibility legislations much earlier to the recommendations of the Twelfth Finance Commission. The current economic slowdown is partially the reason for this. However, even before the visible impact of the economic slowdown on government revenues became visible, the central finances did not look like achieving the fiscal responsibility targets by the stipulated time line of 2008-09. In the presence of the economic slowdown, there will be further pressure on the central deficit and debt because the central government has the larger responsibility for maintaining macro economic stability. The objective of macro stabilization has not been incorporated in designing the fiscal responsibility legislations in India so far. This requires a reworking of the FRBMs of the centre and the states in a framework where stabilization can be attempted in a coordinated way.

e.  'Other' Recommendations of the Finance Commissions

Apart for the substantive recommendations concerning the devolution of funds, the Finance Commissions, particularly the recent ones, have been making several other recommendations or suggestions that have a bearing on maintaining good fiscal relations between the centre and the states. In this context, the Eleventh Finance Commission had observed (Para 12.15 of the Report) "..., the Finance Commission makes recommendations having financial and non-financial implications. Those which have a direct bearing on the outflow or inflow of funds are generally implemented. The implementation of non-financial recommendations should be given equal weight as these also have an impact on the financial position of the centre and states". The central government, however, has not paid much attention to these. This is not conducive either to maintaining good fiscal relations between the two tiers of government or for facilitating development of a robust system of fiscal transfers. Some of the important such recommendations are listed below. This is only a limited list.

Tenth Finance Commission

(i) Centrally Sponsored Schemes

The Tenth Finance Commission had observed as follows (Para 15.7): "In the area of centre-state relations, there is one specific matter to which we would
like to draw attention. It is the persistence of a large number of centrally sponsored schemes. … Central intervention through such schemes is presumably acceptable to the states because they carry with them additional resources. Their continuance makes for large and sprawling bureaucracies at the centre dealing with what are primarily state subjects - e.g. agriculture, rural development, education and public health. Given adequate decentralization, it should be possible to effect considerable economies in such ministries”.

(ii) Plan and Finance Commission Periods (Para 15.10): "We believe it is important to synchronize the period of recommendations of a Finance Commission with that of a five year plan …. the issue is urgent and should be dealt with while determining the period for the next plan”.

(ii) Permanent Secretariat (Para 15.15): "We are in full agreement with what the Eighth Commission had recommended and urge that a full fledged division, appropriately staffed, and with adequate technical expertise be created at the earliest, ……".

**Eleventh Finance Commission**

(a) Synchronization of the period of Five Year Plans with the period of Finance Commission

The Commission had observed as follows (Para 12.8): " .... in the absence of such synchronization, there are practical difficulties in the estimation of committed liabilities of plan schemes, provision for maintenance of assets, estimation of plan revenue expenditure for the forecast period, and so on.".

(b) Creation of Permanent Finance Secretariat (Para 12.10): "There is a need to have a permanent secretariat with a core research staff … to ensure an up to date building of data base on central-state finances, and documentation which could be used by the Commission when it is constituted”.

**Twelfth Finance Commission**

(a) Permanent Secretariat for the Finance Commission

The Twelfth Finance Commission has observed as follows (Para 14.6) " In our view, bulk of problem faced by successive Finance Commissions can be overcome by providing for a permanent secretariat for the purpose of doing the preliminary work both in terms of collecting data and organizing research.
We therefore recommend that the Finance Commission Division should be converted into a full fledged department serving as the permanent secretariat for Finance Commission. Legally and constitutionally there is no uniformity in putting such an arrangement in place.

(b) Financial Autonomy for Finance Commissions (Para 14.7): "..... Another important issue which needs attention is the lack of financial autonomy for the Finance Commissions. All their financial needs have to be cleared by the Ministry of Finance, which acts as the nodal ministry in the government in respect of the Finance Commission. This results in references, back references, delays, especially due to Finance Commission's work receiving a relatively low priority. ..... We, therefore, recommend that the secretariat of the Finance Commission should be vested with the powers of a full fledged department of the government with Ministry of Finance only as its nodal ministry for the purpose of linkage with the Parliament".
References


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The Pioneer, February 10, 1988

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Annexure 1

The Constitution (Eightieth Amendment) Act, 1999

Statement of Objects and Reasons appended to the Constitution (Eighty-Ninth Amendment) Bill, 2000 which was enacted as the Constitution (Eightieth Amendment) Act, 2000.

Statement of Objects and Reasons

1. The Tenth Finance Commission had submitted its report on the 26th November, 1994 for the period of five years, i.e., from 1995-96 to 1999-2000. The said report was laid on the table of both the Houses of Parliament on the 14th March, 1995. One of the recommendations of the Commission that has been under consideration of the Government is an alternative scheme of sharing of the proceeds of certain Union taxes and duties between the Union and the States.

2. The alternative scheme envisages that twenty-six per cent out of the gross proceeds of Union taxes and duties (excluding stamp duty, excise duty on medicinal toilet preparations, Central Sales Tax, Consignment tax, cesses levied for specific purposes under any law made by Parliament and Surcharge) is to be assigned to the States in lieu of their existing share in income-tax, basic excise duties, special excise duties and grants in lieu of tax on railway passenger fares.

3. In addition, three per cent share in the gross proceeds of all Central taxes and duties (excluding stamp duty, excise duty on medicinal/toilet preparations, Central Sales Tax, Consignment tax, cesses levied for specific purpose under any law made by Parliament and Surcharge) is to be assigned to the States in lieu of their existing share in Additional Excise Duties in lieu of Sales Tax on tobacco, cotton and sugar. The commission had proposed that tobacco, cotton and sugar may continue to be exempt from Sales Tax and the Additional Excise Duties in lieu of Sales Tax on these items may be merged with the Basic Excise Duties.

4. Whether the alternative scheme would be more gainful to the Centre or to the States vis-à-vis existing arrangements would entirely depend on the relative growth in the collection of various Central taxes and duties to be pooled.
5. The benefits of the scheme have been listed by the Commission in para 13.2 and 13.3 and 13.18 of their reports. These areas follow:

i) with a given share being allotted to the States in the aggregate revenues from Central taxes, the States will be able to share the aggregate buoyancy of Central taxes;

ii) the Central Government can pursue tax reforms without the need to consider whether a tax is sharable in the states or not;

iii) the impact of fluctuations in Central tax revenues would be felt alike by the Central and the State Governments;

iv) should the taxes mentioned in Articles 268 and/or 269 from part of this arrangement, there will be greater likelihood of their being tapped;

v) the progress of reforms will be greatly facilitated if the ambit of tax sharing arrangement is enlarged so as to give greater certainty of resource flows to, and increased; and

vi) flexibility in tax reform.

6. The above scheme recommended by the Commission is in national interest as it helps to remove a perceived inter-tax in the tax mobilisation effort of the Government of India while leaving sufficient flexibility for meeting Centre’s exclusive needs by keeping Cesses and Surcharges outside the pooling arrangement.

7. A Discussion Paper bringing out various aspects of the scheme was laid on the table of both the Houses of Parliament on the 20th December, 1996 with a view to generate an informed debate.

8. On the basis of a consensus reached in the Third Meeting of the inter-State Council held on the 17th July, 1997, the then Government had agreed in principle to accept the scheme recommended by the Tenth Finance Commission subject to certain modifications.

9. The Government had decided to ratify the decision taken by the previous Government according in principle approval for the scheme recommended by the Tenth Finance Commission with some modifications.
10. Firstly, the percentage share of State is to be reviewed by the successive Finance Commissions instead of freezing it for fifteen years as suggested by the Tenth Finance Commission.

11. Secondly, Government had decided to change the sharing of “gross proceeds” as recommended by the Tenth Finance Commission to the sharing of “net proceeds” in order to maintain consistency between Articles 270, 279 and 280 of the Constitution. However, this will not result in any consequent loss to the States because the Government has also simultaneously decided to compensate the States by suitably enhancing the percentage share beyond 29 per cent.

12. Thirdly, as intended by the Commission, no amendment is sought to be done in article 271, which authorize the Central Government to levy surcharge on Central taxes and duties for the purpose of the Union.

13. The scheme will be effective from 1st April, 1996. The percentage share of net proceeds during 1996-97 to 1999-2000 will be such that the States’ share is 29 per cent of the gross proceeds. The recommendations of the 11th Finance Commission, which has been mandated to give its final report by 30th June, 2000, will cover the 5 years period w.e.f. 1st April, 2000.

14. In order to implement this decision, this Bill seeks to amend Articles 269, 270 and 272 of the Constitution so as to bring several Central taxes and duties like Corporation tax and Customs duties at par with personal income-tax as far as their constitutionally mandated sharing with the States is concerned.
The Constitution (Eightieth Amendment) Act, 2000
[9th June, 2000]

An Act further to amend the Constitution of India.

BE it enacted by Parliament in the Fifty-First Year of the Republic of India as follows:-

1. Short title: This Act may be called the Constitution (Eightieth Amendment) Act, 2000.

2. Amendment of Article 269: In Article 269 of the Constitution, for Clauses (1) and (2), the following clauses shall be substituted, namely:

(1) Taxes on the sale or purchase of goods and taxes on the consignment of goods shall be levied and collected by the Government of India but shall be assigned and shall be deemed to have been assigned to the States on or after the 1st day of April, 1996 in the manner provided in Clause (2).

Explanation—for the purposes of this clause:

(a) the expression “taxes on the sale or purchase of goods” shall mean taxes on sale or purchase of goods other than newspapers, where such sale or purchase takes place in the course of inter-State trade or commerce;

(b) the expression “taxes on the consignment of goods” shall mean taxes on the consignment of goods (whether the consignment is to the person making it or to any other person), where such consignment takes place in the course of inter-State trade or commerce;

(2) The net proceeds in any financial year of any such tax, except in so far as those proceeds represent proceeds attributable to Union territories, shall not form part of the Consolidated Fund of India, but shall be assigned to the State within which that tax is leviable in that year, and shall be distributed among those States in accordance with such principles of distribution as may be formulated by Parliament by law.

3. Substitution of new article for Article 270:
For Article 270 of the Constitution, the following article shall be substituted and shall be deemed to have been substituted with effect from the 1st day of April, 1996, namely taxes levied and distributed between the Union and the States:

(1) All taxes and duties referred to in the Union List, except the duties and taxes referred to in Articles 268 and 269, respectively, surcharge on taxes and duties referred to in Article 271 and any cess levied for specific purposes under any law made by Parliament shall be levied and collected by the Government of India and shall be distributed between the Union and the States in the manner provided in Clause (2).

(2) Such percentage, as may be prescribed, of the net proceeds of any such tax or duty in any financial year shall not form part of the Consolidated Fund of India, but shall be assigned to the States within which that tax or duty is leviable in that year, and shall be distributed among those States in such manner and from such time as may be prescribed in the manner provided in Clause (3).

(3) In this article, “Prescribed” means –

(i) until a Finance Commission has been constituted, prescribed by the President by order, and

(ii) after a Finance Commission has been constituted, prescribed by the President by order after considering the recommendations of the Finance Commission.

4. (1) Omission of Article 272: Article 272 of the Constitution shall be omitted.

(2) Notwithstanding anything contained in sub-section (1), where any sum equivalent to the whole or any part of the net proceeds of the Union duties of excise including additional duties of excise which are levied and collected by the Government of India and which has been distributed as grants-in-aid to the States after the 1st day of April, 1996, but before the commencement of this Act, such sum shall be deemed to have been distributed in accordance with the provisions of Article 270, as if Article 272 had been omitted with effect from the 1st day of April, 1996.

(3) Any sum equivalent to the whole or any part of the net proceeds of any other tax or duty that has been distributed as grants-in-aid to the States after the 1st day of April, 1996 but before the commencement of this Act shall be deemed to have been distributed in accordance with the provisions of Article 270.
Annexure 2

The Constitution (Eighty-Eighth Amendment) Act, 2003
[15th January, 2004.]

An Act further to amend the Constitution of India.

BE it enacted by Parliament in the Fifty-fourth Year of the Republic of India as follows:-

1. Short title and commencement - (1) This Act may be called the Constitution (Eighty-eighth Amendment) Act, 2003.

(2) It shall come into force on such date as the Central Government may, by notification in the Official Gazette, appoint.

2. Insertion of new Article 268A - After Article 268 of the Constitution, the following article shall be inserted, namely:-

Service tax levied by Union and collected and appropriated by the Union and the States.

268A. Service tax levied by Union and collected and appropriated by the Union and the States-(1) Taxes on services shall be levied by the Government of India and such tax shall be collected and appropriated by the Government of India and the States in the manner provided in clause (2).

(2) The proceeds in any financial year of any such tax levied in accordance with the provisions of clause (1) shall be:

(a) collected by the Government of India and the States;

(b) appropriated by the Government of India and the States,

in accordance with such principles of collection and appropriation as may be formulated by Parliament by law.”.

3. Amendment of Article 270. - In Article 270 of the Constitution, in Clause (1), for the words and figures “Articles 268 and 269”, the words, figures and letter “Articles 268, 268A and 269” shall be substituted.

4. Amendment of Seventh Schedule. - In the Seventh Schedule to the Constitution, in List I-Union List, after entry 92B, the following entry shall be inserted, namely:-

“92C. Taxes on services.”

T.K. VISWANATHAN
Secy. to the Govt. of India
Annexure 3

Excerpts from the Report of the Ninth Finance Commission on the Relative Scope of Articles 275 and 282 (Para 7.9)

“Coming to the determination of each State’s need for aid under Article 275, we must make it clear that under this Article, the Finance Commission is obliged to recommend the grants-in-aid of revenue to States and, therefore, the grants for financing the state Plans are very much within the purview of the Commission under the said Article. In fact there is a view that all grants to the states could be channeled through Article 275 only, Mr. K. K. Venugopal an expert on Constitutional law opined before us that Article 282 is clear and unambiguous and unless the Article is re-written with the addition and subtraction of words it would not be possible to arrive at the conclusion that Article 282 is an independent source of power vesting the Central government a discretion to make grants to states for special purposes. As against this, Mr. N.A. Palkhivala opined –

“Article 282 is not intended to enable the Union to make such grants as fall properly under Article 275. Article 282 embodies merely a residuary power which enables the Union or s state to make any grant for any public purpose, irrespective of the question whether the purpose is one over which the grantor has legislative competence.”

Thus, according to Mr. Palkhivala residuary power of grants for public purposes vests under Article 282 in the Union and the state governments. We may also refer to the commentary of Dr. D.D. Basu on constitution of India, 6th edition, volume ‘K’ page 312.

“There is no limit to the grants which can be made by the Union under Article 282 and, in fact, the volumes of grants to the states under Article 282 vie with those made under Article 275. Thus, in 1979-80, while the states received Rs. 375 crore through the Finance Commission, the sum received through the Planning Commission amounted to Rs. 3159 crore. This is striking in view of the fact that Article 282 is a residual provision regarding grants-in-aid.”

Thus opinions on this issue differ widely. The Commission considers it unnecessary to involve itself in the controversy relating to the precise limits on the scope of Article 282 vis-à-vis Article 275. But we are quite certain that if our constitutional obligations
under Article 280 read with Article 275 require us to enlarge the scope of grants beyond the non-plan account limitations, we should not hesitate to do so. We are convinced that such a situation exists now. This is result of a combination of two major factors. The first is the vast disparity among states in size of the non-plan revenue account position. The other is the fact that the Gadgil formula has no linkage to the non-plan revenue account position or the overall financial position of state governments. As yet, there is no formal channel through which additional assistance could be extended to those states whose non-plan revenue accounts have no surplus and whose shares of Gadgil formula grants are substantially less than their approved borrowing to meet a good part of their revenue plan requirements and this set in motion a vicious circle which, ultimately, may invalidate the very concept of balance regional development. We propose to introduce a mechanism to correct this basic flow in the present system of federal fiscal transfers. We are clear in our mind that Article 275 provides full constitutional support for such a new arrangement.

Shri Justice A.S. Qureshi, member has opined that Article 275 is the only source for giving grants-in-aid to states. He has elaborated his view on this issue in his “Note of Dissent”.

Study on Functioning, Structure of Local Governance in North Eastern Region with Special Reference to Autonomous District Councils/Autonomous Regional Councils

North-Eastern Hill University
2009
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Conclusion 

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Annexure Letter from North-Eastern Hill University
1. Introduction

Independent India’s members of the Constituent Assembly made a significant contribution to the tribal people of the North East by making provision in the Constitution of India that the life and culture of these people be preserved. To this end was incorporated the Sixth Schedule in the Constitution.

The tribal people in the plains and hills of composite Assam were given the option of setting up Autonomous District Councils (ADC) under the provisions of the Sixth Schedule. District Councils were set up for the Karbis, Mikirs, Garos, Khasis, Jaintias, Mizos. When Assam was reorganized with the emergence of hill states several of these Autonomous District Councils remained, and as in the case of the Mizos they no longer had requirement of the ADC. In more recent times, ADC’s has been provided to smaller communities in Mizoram and in Tripura. Similarly the Bodos of Assam have been provided a Council similar to the Darjeeling Gorkha Council.

Several of the Councils have exercised the legislative, judicial and executive powers vested in them to meet the expectations of the people and the State that these Councils are located. The functioning of the ADC however, has been coming up for scrutiny both by Government and civil society. The situation today is that several of the ADC have moved away from the mandate given to them by the Constitution and become another of the development agencies. The reason for their establishment and functioning apparently is not a serious issue with the members of the Autonomous District Councils.

It is timely that the Government of India is examining the functions of the Autonomous District Councils and the Autonomous Regional Councils. Perhaps this is being done not with the intention that the numbers of the ADC and the Regional Autonomous Councils increase in number but with the desire to strengthen the functioning of these institutions.

The Ministry of Home Affairs, Government of India has constituted the Commission on Centre-State Relations under the Chairmanship of Justice M. M. Punchhi, former Chief Justice of India to undertake a comprehensive review of the issues concerning Centre-
State relations and to make recommendations thereon. As part of the review of the terms of reference of the Commission in association with the North Eastern Council organised a workshop on “Local Government and Decentralization Planning and Governance” at Pinewood Hotel, Shillong, 30 September 1 October 2008. The Commission wanted to provide a process of deliberation and access viewpoints of various segments. Of relevance to this Report were the discussions on the first day of the meet on one of the terms of reference of the Commission- “Many of the regions falling in the scheduled areas (Schedules V and VI) have traditional institutions of governance coexisting with or substituting Panchayati Raj Institutions e.g. Autonomous Hill Councils etc. What are your views as to how these institutions can be further strengthened and be congruent with the spirit of the 73rd and 74th amendments without undermining their traditional character?” This was discussed in a session “Functioning of District Autonomous Councils and Regional Autonomous Councils and Decentralized Planning and Governance.” Policy makers and representatives of a cross section of the autonomous district councils and territorial councils were present and participated.

Following the workshop a meeting was held on 10 October 2008, in the office of Shri V. K. Duggal, Member of the Commission on Centre-State relations and attended by Prof. N. R. Madhav Menon, Member of the Commission; Shri Ravi Dhingra, Secretary of the Commission; Smti Veena Upadhay, Additional Secretary and Adviser to the Commission; to which Prof. Pramod Tandon, Vice-Chancellor, North-Eastern Hill University and Prof. David R. Syiemlieh, Controller of Examinations, NEHU were invited.

At the meeting it was decided to request and make provision of a grant to the North-Eastern Hill University as nodal agency, to conduct a study for the Commission on Centre-State Relations relating to the Autonomous District Councils/Regional Councils and related issues in those parts of the region where these patterns of local governance are in place and where other patterns of local governance exist. Prof. David R. Syiemlieh, was requested be the Coordinator of the Study.

After further discussion the terms of reference of the proposed study was accepted.

**Terms of Reference**

(a) A critique of the powers, including discretionary powers of the Governors with regard to the Autonomous District Councils (ADC’s) and Autonomous Regional Councils (ARC’s) as Provided under the Sixth Schedule as also an empirical analysis of the exercise of these powers.
(b) An assessment of the exercise of Judicial powers of ADC’s and ARC’c as conferred under clauses 4 & 5 of the Sixth Schedule in the light of some illustrative case studies as also a study of the Implications of conflicts between State Law Enforcement Agencies and ADC’s; Impact of 1953 Justice Rules, and 1957 Justice Rules.

(c) Role of ADC’s and ARC’c in Planned Development and Identification of priority areas for capacity building for various functions.

(d) Common Minimum Consistency and Parity (CMCP) in the function/ responsibilities, assigning of functionaries, and devolution of funds, including mobilization of resources through levy of taxes etc, and mode of fund flow.

(e) Areas of enhancement of autonomy in the light of 73rd and 74th Amendments and some features of Panchayati Raj Extension to Scheduled Areas (PESA), 1996 (the reference is to some features of PESA, which is otherwise applicable to Fifth Schedule Areas, with the express objective of enhancement of autonomy for ADC’s and ARC’c in Sixth Schedule Areas, appoint made by the then Secretary, Ministry of Panchayati Raj during her presentation to the Commission).

(f) Provision for two/three tiers of local governance and interface between ADC’s and Village Councils (including extant traditional institutions e.g. Dorbars and Syiem), between ADC’s and Deputy Commissioner, and between ADC’s and State governments.

2. The appropriateness of the Nagaland model of communitization based on Village Councils and Village Development Boards.

The work for the study really got away on the early part of the year with the sanction of the grant for the study.

A team of researcher and scholars of the region prepared the collection of data and conducted interviews where necessary. A core Team analyzed the material collected within the terms of reference and prepared the Report. These included:

1. Prof. L.S.Gassah, Political Science Department, North- Eastern Hill University, Shillong, Meghalaya.

2. Dr A K Thakur, Reader, History Department, North-Eastern Hill University, Shillong, Meghalaya.
3. Shri Uttam Bathari, Assistant Director, Indian Council for Historical Research- North Eastern Regional Centre, Guwahati, Assam.

4. Shri Nabajyoti Bathari, Lecturer, Political Science Department, Haflong Government College, Haflong, Assam.

5. Dr. Sukhendu Debbarma, Reader and Head, History Department, Tripura University, Agartala.

6. Dr. Luke Daimari, Senior Lecturer in History, Nehru College, Pailapool, Silchar, Assam.

7. Prof. Pura Tado, Political Science Department, Rajiv Gandhi University, Itanagar, Arunachal Pradesh.


9. Mr.Kedilezo Kikhi, Lecturer, Department of Sociology, Nagaland University, Kohima, Nagaland.

10. Dr.Jankhongam Doungel, Senior Lecturer, Department of Political Science, Government Lawngtlai College, Lawngtlai, Mizoram.

11. Mr. Jyotirmoy Chakma, Lecturer, Department of History, Kamalnagar college, Kamalnagar, Mizoram.

12. Dr. Hmingthanzuala, Senior Lecturer, Department of Political Science, Saiha Government College, Saiha, Mizoram.

13. Dhiraj Kumar Borkotoky, Study Research Assistant, North Eastern Hill University, Shillong.

14. Mr. Debajyoti Das, Doctoral Scholar, School of Asian Studies, University of London, presently on field study in Nagaland.

15. Prof. David R Syiemlieh, Controller of Examinations, North-Eastern Hill University, Shillong, Coordinator.

Gratefully acknowledged is the support of Dr. C. J. Thomas Acting Director, Indian Council of Social Science Research- North Eastern Regional Centre, Shillong.
Background study

The administration of the tribal areas of the North-Eastern region which were earlier known as “Backward Tracts”, has a history of its own. The Grant of the Diwani of Bengal to Robert Clive in 1765 by Shah Alam II, secured for the East India Company ‘superintendence of all revenues’ in the presidency of Bengal, which at that time consisted of Bengal, Bihar, Orissa and Assam.

In the subsequent years, many Acts, Rules and Regulations were passed from time to time which had affected the North-Eastern region in diverse ways. Few of these Acts may be mentioned like – the Scheduled Districts Act of 1874, the Government of India Acts, 1919 and 1935. Under the scheme of Provincial autonomy, the hill areas of the then Province of Assam fell into the categories, namely, the Excluded and Partially Excluded Areas, as scheduled in by the Order-in-Council under the Government of India Act, 1935. The main concern of the British administration at that period of time was more static than dynamic. Thus the administrative insulation contributed to the prolongation of backwardness of the North-Eastern region especially the areas predominantly inhabited by the tribal people. The British did everything possible to check the emotional integration between the tribal and non-tribal population for the evolution of a spirit of common identity superseding ethnic diversities. There were even abortive attempts at keeping the tribal areas of the region outside the Indian Dominion when the Indian Independence Act of 1947 was being passed by the British Parliament.

When India attained its independence in 1947 and adopted its Constitution in 1950, it envisaged strong democratic institutions at the grass-root level as well as concerning the day-to-day affairs of the tribal communities. Consequently, democratic decentralization and the establishment of Panchayati Raj institutions is one of the Directive Principles of State Policy. However, in the case of the Tribal Areas, especially those in the North-East, there are certain special provisions provided in the Constitution itself. The framers of the Indian Constitution also recognized the necessity of a separate political and administrative structure for the hill tribal areas of the erstwhile State of Assam by enacting the Sixth Schedule to the Constitution of India under Articles 244(2) and 275(1). In doing so, they were guided broadly speaking by three major considerations:

(i) The necessity to maintain the distinct customs, socio-economic and political culture of the tribal people of the region and to ensure autonomy of the tribal people and to preserve their identities;
(ii) The necessity to prevent their economic, social and political exploitation by the more advanced neighbouring people of the plains; and

(iii) To allow the tribal people to develop and administer themselves according to their own genius.

The constitutional provisions therefore seek to maintain and safeguard the tribal customs, traditions, culture, language, social and traditional councils/institutions and courts, and to secure the autonomy of the districts which are inhabited by fairly homogenous groups of tribal communities.

The Bordoloi Sub-Committee

It was rather fortunate, on the one hand, for the tribal areas of North-East India because the Interim Government of India (which was set up in 1947) could realize the critical situation and the political aspirations of the people of the hill areas/districts of the then composite State of Assam. The Interim Government also showed some kind of positive interest in the problems of the tribal areas of North-East India and wanted to look into their grievances and affairs so as to enable them to participate in policy and decision-making process and manage their affairs according to their genius and pertaining to their welfare.

Against this background, the Interim Government appointed a Sub-Committee of the Constituent Assembly known as the North-East Frontier (Assam) Tribal and Excluded Areas Committee under the chairmanship of Gopinath Bordoloi, the then Chief Minister of Assam. This Sub-Committee, popularly known as the Bordoloi Sub-Committee visited a number of the hill districts and carried on the spot study of the traditional institutions of the tribal communities of North-East India.

In its Report, the Bordoloi Sub-Committee, broadly speaking, took three factors into consideration while proposing a separate scheme of administration for the tribal areas of North-East India. The scheme it recommended led to the setting up of the Autonomous District Councils. These factors are:

1. The distinct social customs and tribal organizations of the different tribal communities as well as their religious beliefs;

2. The exploitation by the people of the plains on account of the latter’s superior organization and experience of business; and
3. The fear that unless suitable financial provisions were made, or powers were conferred upon the local councils themselves, the Provincial Government might not, due to the pressure of the people of the plains, set apart adequate funds for the development of the tribal areas.

The Sub-Committee further felt that the assimilation of the people of the tribal areas with the rest of the country would not take place by the sudden breaking up of the tribal institutions; what was required was the evolution of growth on the old foundations. This meant that the evolution should come, as far as possible from the tribals themselves and it was equally clear that contact with outside institutions was necessary, though not in a compelling way.

To fulfill the terms of reference given to the Sub-Committee, it visited the tribal areas of the hill districts of the then composite State of Assam and interacted with the representatives and heads of the different traditional institutions in order to enable it to formulate a model administrative set up for these areas within the State of Assam. When the members of the Sub-Committee studied the problems and issues involving the administration of the tribal areas and their people, it realized that these areas needed protection and safeguard so that they might be able to protect and preserve their way of life and at the same time participate in the political life of the country along with others.

The members of the Sub-Committee also noted the existence and continuation of the traditional tribal self-governing bodies/institutions which functioned more or less democratically and settled their disputes in accordance with their own traditions, customs and usages of the land. The Sub-Committee therefore sought to evolve a system by which it would be possible to remove the apprehensions of the tribal people of the region, simple and backward as they were, so that they might not be exploited, subjugated and oppressed by the more advanced people who are their nearest neighbours.

The recommendations of the Bordoloi Sub-Committee were debated and discussed threadbare by the members of the Constituent Assembly in 1949. It was quite unfortunate, had it not been for the constructive and strong defensive stand and positive approach taken by the tribal leaders like Dr. Ambedkar, Rev. J. M. Nichols-Roy and Jaipal Singh as well as Gopinath Bordoloi himself because of the negative stand and indifferent attitudes shown by many non-tribal members of the Constituent Assembly. Mention may be made specially on the negative stand and indifferent attitudes of the two members from Assam, Kuladhar Chaliha and Rohini Kumar Choudhury towards the issue of the hill areas’ autonomy during the course of the discussion in the Constituent Assembly. Such indifferent attitude
and detestation towards the hill areas’ autonomy by the two leaders could be clearly understood through their expressed opinions while taking part in the Constituent Assembly Debate (dated 5th-7th September 1949) relating to the draft provisions of the Sixth Schedule put forward by the Bordoloi Sub-Committee. However, all such negative views were finally rejected by the Constituent Assembly.

The recommendations of the Bordoloi Sub-Committee were incorporated in the Sixth Schedule to the Indian Constitution. The idea behind the Sixth Schedule was to provide the tribal people with a simple and inexpensive administration of their own, so that they could safeguard their own customs, traditions, culture, language, etc., and to provide them maximum autonomy in the management of their tribal affairs. The Bordoloi Sub-Committee in particular, appreciated that the tribal people were particularly sensitive about their lands, forests, traditional system of justice and social customs. Most of the recommendations of the Bordoloi Sub-Committee were accepted. This therefore led to the incorporation of the Sixth Schedule into the Indian Constitution and provided for the constitution of the Autonomous District Councils (ADC’s) in certain hill districts of the then composite/undivided State of Assam. Thus such ADC’s were introduced in certain hill districts (except in the Naga Hills district) in 1952 and in 1953, a Regional Council was introduced in the Mizo Hills district which was meant to serve the needs of the smaller communities among the Mizos like the Pawis, the Lakhers and the Chakmas under the Sixth Schedule to the Indian Constitution. In 1972, the same Regional Council was up-graded into the ADC, one each for the Pawis, the Lakhers and the Chakmas. These ADC’s have functioned in their respective autonomous districts for the last fifty seven years. Many of them have passed from time to time a number of Acts, Rules and Regulations as empowered to them under the provisions of the Sixth Schedule. Such Acts, Rules and Regulations are dealing with and affecting the people of their respective areas in diverse ways, relating to such pertinent issues like the appointment and succession of chiefs and village headmen, land, forest, primary school education, planning processes, markets, trade and commerce, developmental activities, etc. to mention a few of them. Some such Acts have direct effects on the traditional institutions like the chiefs and their councils.

Examining the role of the ADC from another angle, it may be noted that it was an institutional innovation of effecting decentralization of power at the district level covering under its general framework the problems and issues down to the village level as devolved under the Constitution of India. However, soon after the setting up of the ADC’s in the
Sixth Schedule areas of North-East India, these Councils had been seriously and persistently voicing their grievances against the treatment meted out to them by the different State governments, where the ADC’s are in existence, in the matters of provision of Grants and other financial assistance, according of approval of the legislative proposals of the ADC’s, nomination of members to the ADC’s, supersession of the ADC’s, etc.

Before the Re-organization of the then undivided State of Assam (pre- 1972), such grievances were directed against that State. The situation is not so different today even after the re-organization of Assam which gave way to the creation/formation of full-fledged States like Meghalaya, Mizoram, Tripura, etc. For instance, in Meghalaya today, a tug-of-war is still continuing between the State Government and the three ADC’s over a particular paragraph (Paragraph 12A) of the Sixth Schedule. The ADC’s in Meghalaya are unhappy and dissatisfied with the decisions of the State Government which makes use of the certain paragraph to declare those Acts, Rules, Regulations passed by the ADC’s null and void on the basis of the strength of this paragraph.

The ADC’s were created in certain hill areas/districts of North-East India in response to the constitutional needs of the tribal people for autonomy due to their apprehensions about the preservation and protection of their ethnic identity and their rights over the lands, natural resources, forests, customary laws, languages/dialects, traditions, etc. The Autonomous District Councils were conceived and delivered to ensure the right of self-governance of the tribal people, to enable them to manage their affairs according to their own genius, to enable them to preserve and protect their ethnic identity and to face the forces of assimilation squarely from their more advanced neighbours in the plains.

The underlying factor contributing to whatever achievements of the ADC’s is the tribal people’s emotional and active involvement in asserting their rights of self-governance and to run the administration by their own elected tribal representatives for promoting, preserving and protecting their rights over their lands and natural resources which are so dear to them to their own hearts and the over-all economic interests and development of their own people in general. No wonder, the concept of the ADC has served as the basic model for meeting the demands for autonomy.

The autonomy of the ADC’s has been much affected in the area of financial independence. They have to depend on their respective State governments in matters of financial allotments. This in turn has reduced and restricted their autonomy and performance. One of the sources of finance of the ADC’s is the share of royalty accruing each year from
licenses and leases for the purpose of prospecting for or extraction of minerals granted by
the State Government in respect of any area within an autonomous district. For instance,
in Meghalaya, all the three ADC’s have complained that they are not given due share from
the collection of royalties and taxes. Secondly, the ADC’s alleged that because of the
obstructive attitude of the State Government in the matter of the release of funds, they
have been forced to adopt undesirable practices so as to raise funds in order to discharge
their constitutional obligations like running of Primary Schools, Dispensaries and even
to meet the salaries of the employees of the Councils.

The Sixth Schedule confers few development functions on the ADC’s, though there is an
enabling clause whereby the State Government can entrust such functions with them.
On the event of the re-organization of States in North-East India in 1971, there was
some sort of understanding at the political level as a result of which a number of
development functions were conferred on the ADC’s. In this aspect, certain ADC’s in
North-East India experienced subsequently that this arrangement was a fragile one. Lacking
in statutory support, the ADC’s had to depend on the changing political relations with the
State leadership. The developmental activities of the ADC’s therefore depend very much
on the political party or parties that run the State administration. If the same political
party or alliance of parties is in power both at the State and District Council level, the
latter may have a smooth sailing in its programmes of developmental activities due to a
good understanding at the political or party level. Funds or flow of funds from the State
Government to the ADC’s may not be a problem. If it is otherwise, a number of obstacles
and hurdles may be created by the party or parties/alliances in power at the State level to
jeopardize the plan of action that might be framed by the ADC’s for the development of
the autonomous districts.

Dissolution of ARC

A significant feature of the Sixth Schedule is the provision for the constitution of Regional
Councils by the Governor within an Autonomous District Council to enable a small yet
distinctive tribe living in a compact area to enjoy the same degree of autonomy as the
larger closely-knit tribe in the District Council. The Governor also has the power to
determine the area and boundaries of the Regional and the District Councils. The provision
recognizes the diversity of the tribes, the need to protect smaller ones from possible
domination by the larger tribe and therefore to empower them with full autonomy to
preserve their culture and customs and to administer their areas for their betterment.
Thus the legislative and administrative powers of the Regional and District councils are the same, the latter in no way being superior. The administration of justice under the customary laws and all other legal and administrative responsibilities in regard to land, forests, water courses, village councils, village *hats*, regulation of trade by non-tribal’s, shifting cultivation are discharged by the Regional Council by its own machinery, and are independent of the District Councils. At present there are no Regional Councils in any of the four North Eastern states where the Sixth Schedule is in operation. The Mizo district of erstwhile Assam had a regional council for the Pawi-Lakher tribes. Later with the grant of the Union Territory status, Pawi Lakher Regional Council was trifurcated into three Regional Councils namely, Pawi Regional Council, Chakma Regional Council and Lakher Regional Council on 2 April 1972. They were subsequently upgraded to the status of Autonomous District Council on 29 April 1972. Despite the identification of Lai as “Pawi” and Mara as “Lakher” in Mizoram, the Lais and the Maras regarded the popular terms “Pawi” and “Lakher” as derogatory terms. They demanded change of their District Council names after their ethnic and original name. Thus, under the Sixth Schedule to the Constitution (Amendment) Act, 1988 of Indian parliament (No. 67 of 1988). The Pawi Autonomous District Council was changed into Lai Autonomous District Council and the Lakher Autonomous District Council into Mara Autonomous District Council.

The following are the Autonomous District Councils in the region

1. Khasi Hills Autonomous District Council, covering three districts of the State of Meghalaya, with HQs at Shillong.
2. Jaintia Hills Autonomous District Council covering one district of the State of Meghalaya with HQs at Jowai.
3. Garo Hills Autonomous District Council covering three districts of the State of Meghalaya with HQs at Tura.
4. North Cachar Autonomous District Council covering one district of the State of Assam with HQs at Haflong.
5. Karbi Anglong Autonomous District Council covering one district of the State of Assam with HQs at Diphu.
6. Lai Autonomous District Council, Mizoram with HQs at Saiha.
7. Mara Autonomous District Council, Mizoram with HQs at Lawngtlai.
8. Chakma Autonomous District Council, Mizoram, with HQs at Chawngte also known as Kamalanagar by the Chakma people.

9. Tripura Tribal Areas Autonomous District Council covering several districts of Tripura inhabited by indigenous tribals; its Council and Assembly are situated in Khumulwng, a town 26 km away from Agartala, the State capital.

10. Bodoland Territorial Council (BTC) was established according to the Memorandum of Settlement of February 10, 2003. BTC was announced to be formed just after the surrender of the BLTF. The BLTF under the leadership of Hagrama Mohilary laid down their weapons on 6 December 2003. Shri Hagrama was sworn in as the Chief Executive Member (CEM) on December 7, 2003. The BTC with HQs at Kokrajhar, initially had 12 electorate members each looking after a specific area of control call Somisthi. The area under the BTC jurisdiction is called the Bodo Territorial Autonomous District (BTAC). The BTAC consists of four contiguous districts—Kokrajhar, Baska, Udalguri and Chirang—carved out of eight districts—Dhubri, Kokrajhar, Bongaigaon, Barpeta, Nalbari, Kamrup, Darrang and Sonitpur—an area of 27,100 km² (35% of Assam).

Autonomous Councils in Assam and Manipur other than under the 6th Schedule

In the State of Assam there are State level Councils created by the Government of Assam. These are as follows:

1. Rabha Hasong Autonomous Council (RHAC).
2. Lalung (TIWA) Autonomous Council (LAC).
3. Mising Autonomous Council (MAC).
4. Thengal Kochari Hill Council (TKHC).
5. Sonowal Kochari Council (SKC).
6. Deori Council (DC).

The first three of these councils were created in the year 1995. The last three were created in the year 2005. The administrative structure of these Councils are patterned on the Autonomous District and the Regional Councils created by the Sixth Schedule. The members of such State Councils feel that the measures provided to them are not enough to protect, preserve and promote their culture and hence there has been constant agitations and protest by the members of these Councils to get them promoted to the Sixth Schedule.
status. The Government of Assam also has been playing with the emotions of the smaller communities by promising them with such state level councils, the latest of such community being the Amri Karbis who have been promised with such a council.

In the case of Manipur taking strength form Article 371C of the Constitution of India, the State government has constituted Autonomous District Councils under the Manipur Hill Areas District Councils Act 1971. Six ADC’s were constituted in 1973. These are listed below:

1. Sardar ADC
2. Sardar Hills ADC
3. Churachandpur ADC
4. Ukhrul ADC
5. Tamenglong ADC
6. Chandel ADC

In March 2001 the State Government decided that it had no objection to the extension of the provisions of the Sixth Schedule of the Constitution to the tribal areas of the State with certain local adjustments and amendments. More recently the hill areas of Manipur have started asking for Sixth Schedule status.

Following this introduction and background we may direct our attention on the terms of reference, which are studied separately hereunder.

A. Critique of the powers, including discretionary powers of the Governors with regard to the Autonomous District Councils (ADC’s) and the Autonomous Regional Councils (ARC’s) as provided under the Sixth Schedule as also an empirical analysis of the exercise of these powers.

The Governors of the States which falls under the ambit of the Sixth Schedule, are expected to play a vital role in relation to the functioning of the Autonomous District Councils and the Autonomous Regional Councils. The Governors have been given powers and functions as provided in the Sixth Schedule of the Constitution. The ADC’s and ARC’s were supposed to play a very important role in not only protecting, preserving and promoting the culture, beliefs, values of their region, but also play a vital role in the process of development by including the traditional local self governing institutions within
their ambit. Thus in this scenario the role of the Governor is also very important and hence can hardly be undermined. An analysis of the provisions of the Sixth Schedule clearly shows that the Governor can play a very important role in the effective functioning of the ADC’s and ARC’s. Before going into a critical evaluation of the powers of the Governor it would be helpful for us to know some of the important powers that can be exercised by the Governor under the provisions of the Sixth Schedule.

(a) The Governor can nominate four members in each District Council who hold office at his pleasure. [Paragraph 2(1) and 2(6A)].

(b) The Governor is required to approve the rules made by the District Council and the Regional Council for composition and delimitation of the District and Regional Council, qualification terms of office etc. of its members and generally for all matters regulating the transaction of business pertaining to the administration of the District. [Paragraph 2(7)].

(c) Regulations framed by the District Council for the control of money lending and trading by non-tribals require assent of the Governor to have the force of law. [Paragraph 10(3)].

(d) The Governor may appoint a Commission to enquire into the administration of Autonomous District/Regions. [Paragraph 14(1)].

(e) Report of Commission appointed under paragraph 14 is required to be laid before the State Legislature with the recommendation of the Governor (except in the state of Assam) with respect thereto [Paragraph 14(2)].

(f) The Governor may place one of the ministers in charge of the welfare of the autonomous district/Region in the state. [Paragraph 14(3)].

(g) The Governor may dissolve a District or Regional Council and assume to himself all or any of the functions or powers of the District or Regional Council on the recommendation of the Commission appointed under paragraph 14. [Paragraph 16(1)].

Besides many, the above were some of the powers and functions of the Governor. In spite of the above powers and functions of the Governor, one pertinent question that arises today is how far the Governor has been able to make use of his powers in relation to the ADC’s and ARC’s? Though the Constitution gives the Governor wide range of powers and functions, but in practice the Governor cannot make use of his powers at his
own discretion. The Governor has to act according to the Council of Ministers with the 
Chief Minister as its head in matters relating to the ADC’s and ARC’s. The Constitution 
under Article 163 has tied the hands of the Governor and makes him act on the advice of 
the State cabinet. Thus today we find that the Governor has little say about the functioning 
of the ADC’s and ARC’s of the North Eastern Region.

As it has already been mentioned that the Governor does not play a vital role in the 
ADC’s and ARC’s, which can be substantiated in the following paragraphs. To begin with 
even in the matters of appointing the elected members of the District Councils (MDC’s), 
the Governor of Meghalaya has delegated the power of swearing in the elected members 
of the ADC’S to the respective Deputy Commissioners. The Governor does not even 
address the inaugural sessions of the ADC’s. The Governor has the power to nominate 
four members in each District Council who shall hold office at his pleasure under paragraph 
2(1) and 2(6A) of the Sixth Schedule, but the Governor of the various North Eastern 
states are not consistent in the use of this power as in the case of Meghalaya, this power 
of the Governor has more or less remained dormant and hence the Governor does not 
feel it necessary to utilize this power because of political repercussion from various quarters 
of the State.

The Governor under paragraph 14 of the Sixth Schedule has the power to appoint 
Commission of inquiry into and report on the administration of the autonomous districts 
and autonomous regions. It has been found out that in the various States of North East 
with ADC’s, the Governor has not made use of this provision effectively In the State of 
Meghalaya one such Commission appointed by the Governor in 1982 was the S.K Dutta's 
Commission of Inquiry on Autonomous District Councils in the State of Meghalaya. 
Even after 29 years of the S.K Dutta Commission of Inquiry, no other such Commission 
has been constituted by the Governor to review the functioning of the ADC’s of Meghalaya, 
which may indicate that all is well with the ADC’s. This has been one of the major 
reasons for the deteriorating standard of the ADC’s of Meghalaya as there has been no 
commission to review their administrative setup and discharge of their functions. Even 
the Panchayati Raj Structure was revitalized by the L.M Singhvi Commission through the 
73rd and 74th Amendment of the Constitution; these amendments gave a new dimension 
to the entire concept of democratic decentralization of powers to the rural people in 
India. Thus the Governors of the various states should constitute such Commissions as 
and when required, whose reports would help in redefining the role of ADC’s in relation 
to local self governance. Today there is an ever growing realization that the ADC’s have
not been able to deliver the goods that was expected of them and hence there is a need to
revitalize the ADC’s and here the Governor can play a very important role by constituting
Commissions to overlook the functioning of the ADC’s in the states where the ADC’s are
not performing as is expected of them.

The Governor’s role today has been mainly limited to giving his assent on the bills passed
by the State Legislatures in relation to the ADC’s. There is no doubt that the role of the
Governor is very special in the context of the District and the Regional Councils and
hence there is a need for Governors to be proactive to promote and facilitate local
participative planning on Sixth Schedule areas. Clearly the spirit of the Sixth Schedule is
that the Governors are to function as the custodian of tribal autonomy and hence the
Governors should play a greater and vital role in relation to the ADC’s. Proactive Governors
can be very helpful in uplifting the deteriorating standards of the ADC’s.

The above is a general observation on the role of the Governor in relation to the ADC’s.
We may consider the views from the various ADC’s about the role of the Governor in
relation to their respective ADC’s. Below are the views of some of the ADC’s regarding
the role of the Governor.

(a) **Lai Autonomous District Council in Mizoram**

The discretionary power of the Governor is one of the most problematic issues in
the functioning of the District Council as well as in the District Council relation
with the State Government. It should be noted that the Governor is authorized to
exercise his discretionary powers without consulting the Council of Minister of
State only with respect to subject, mentioned in paragraph 9 sub–paragraph 2 of
the Sixth Schedule to the Constitution of India: The Sixth Schedule to the
for the States of Tripura and Mizoram with respect to exercise of discretionary
powers by the Governor. Thus, it is laid down that the Governor in the discharge of
his function under sub-paragraphs [2] and [3] of paragraph 1, sub-paragraphs [1]
and [7] of paragraph 2, sub-paragraph [3] of paragraph 3, sub-paragraph 4 of
paragraph 4, paragraph 5, sub-paragraph [1] of paragraph 6, sub-paragraph 2 of
Paragraph 7, sub-paragraph 3 of paragraph 9, sub-paragraph 1 of paragraph 14, sub-
paragraph [1] of paragraph 15 and sub-paragraph [1] and [2] of paragraph 16 of this
schedule, shall after consulting the Council of Minister, and if he thinks necessary,
the District Council and Regional Council concerned, take such action as he considers
necessary in his discretion. It is clearly laid down that the Governor shall consult
the Council of Minister and if he thinks necessary, the District Council in the exercise of the above mentioned discretionary powers. In fact, discretionary power has been accorded to the Governor for protection and preservation of minority tribes of the District Council, however discretionary powers had not been judiciously exercised.

A controversy erupted in the District Council area of Mizoram during the tenure of Mr. A.R. Kohli, as Governor of Mizoram. The Lai Autonomous District Council (Constitution and Conduct of Business) Rules, 2002 was said to be made by the Lai Autonomous District Council as per the provision of Paragraph 2, sub-paragraph (7) of the Sixth Schedule to the Constitution of India and the said rule was published in the State Gazette on 21.2.2003 in issue No 38 which was republished in State Gazette on 6.3.2003 in issue No. 58. Moreover, the said rule was supposed to be approved by the Governor of Mizoram on 8.8.2002 as published in the Gazette. However, the then Chairman of LADC, Mr. Manghmunga Chinzhah stated that the said rule was not made and tabled in the legislature of LADC. Subsequently certain loopholes of the Rules were amended by the LADC and it was adopted with effect from 20.10.2003.

It may be recollected that, at the time when the Constitution was being drafted the role of Governor with respect to District Council was hotly debated in the Constituent Assembly. Dr. B.R. Ambedkar clarified that “Whenever the word Governor occurs, it means the Governor acting on the advice of the ministry of state government”. Therefore, the Governor is bound to exercise his discretionary power by consulting the Council of Ministers and the District Council concerned, if necessary. So, the Governor is required to act upon the advice of State Government and District Council with respect to appointment of nominated members and in some other important decisions. The constitutional convention and precedence also demanded that, the role of President in appointment of nominated members in the Lok Sabha and the Rajya Sabha be similar to the role of Governor in the appointment of nominated members in the District Council. As such, the Governor was required to approve the name, suggested by the District Council and State Government for the nominated seats. However, he might have the liberty to exercise his discretion if minority, person with specialized knowledge and women were not included in the suggested list. Thus, constitutional convention, precedence and constitutional practices were grossly violated by the then Governor, Mr. A.R. Kohli in 2002. Mr. A.R. Kohli conducted an interview for appointment of nominated MDCs in Circuit House, Lawngtlai at 2PM on 2nd October 2002 and about 70 aspirants for nominated MDC faced that interview. It was an unusual constitutional practice, which was
against the norm of parliamentary democratic practices. The reason being, it was an attempt to recruit lawmakers of District Council like the recruitment of government servant and it also put a question mark to sanctity of the legislature, because District Council is an effective legislature at the grass-root level, where, tribals practically learn the democratic practices. As such, a provision is required to be provided to prevent the misuse of discretionary power by the Governor.

(b) The views from North Cachar Hills Autonomous Council (NCHAC)

In the administration of the Autonomous District Council, the Governor of the State of Assam has been playing very significant role. Para 20BA of the 6th Schedule to the Constitution of India has conferred the power to the Governor of Assam to exercise at his own discretion in respect of 18 matters. Accordingly though the NCHAC has been vested with enormous power, the Governor of Assam can interfere regarding administration of the Autonomous District Councils if situation arise.

According to the para 1(2) of the 6th Schedule to the constitution of India, the Governor can divide the Autonomous District into Regional Councils for any particular tribe. However, in NC Hills no Regional Council has been created so far, though demand has been made by the Zeme Naga tribe.

The 10th NCHAC has recently passed a bill to change the nomenclature of the district which falls under the discretionary power of the Governor. According to the para 1 (3) to the 6th Schedule to the Constitution of India the Governor can alter the name of any Autonomous District. In this regard, the Governor has to take into the account of the report of the commission constituted for the same purpose. Following this procedure the Governor of Assam has appointed a commission under the chairmanship of the Mr Dinesh Prasad Gowala to asses the bill passed by the Council. However the commission has been submitted the report to the Governor of Assam.

According to para 2(1) of the 6th Schedule, the Governor can nominate four members to the Autonomous Council. Since the inception the Governor of Assam has been appointing four members to this Council. The appointed members remain in the office during the pleasure of the Governor. In the year 1997, the nomination of Shri Nibaran Das was cancelled and in his place Shamal Kanti Dey was nominated by the Governor of Assam. However, in the 10th NCHAC no member has been appointed by the Governor of Assam due to prevailing political instability in the district.
According to sub para 6 of the para 2 the Governor shall make rules for the 1st constitution of the District Council and Regional Council in consultation with existing tribal council. Exercising this power the Governor of Assam framed Assam Autonomous District (Constitution of District Council) Rules 1951. This rule has been adopted by the N.C.Hills Autonomous Council with certain changes and it has clearly mentioned about the composition of District Council and allocation of seats, delimitation of constituencies for the purpose of election and qualifications to be elector.

The sub para 6 of the same para has conferred the power to the Governor for delimitation of the constituency for the purpose of election. In case of the NC Hills delimitation of the constituencies has been done three times so far. Delimitation was first done in 1968 and the strength of the Council was increased from 16 to 24. Among them 4 members were nominated by the Governor and rest were directly elected by the people. Again in 1980, before the 6th election of the NCHAC, the elected constituencies were raised to 23. Finally, in 2007 by the 34th Amendment of the Constitution of the NCHAC, the elected members were again raised to 28.

Under this provision, if any question arises as to whether a member of the Council has become subject to any provision of disqualification, the matter shall be referred to the Governor of Assam and in this regard his decision is final. In the second District Council election Sri Kuloda Hojai was elected from Hajadisa Constituency. His membership was declared null and void by a verdict of the court as he did not have requisite age to be member of the Council. Finally his membership was ceased by the Governor and another member was elected in his place through bye-election.

Exercising the powers conferred by Para 2 sub para 6, the Governor of Assam extended the term of the Seventh District Council of the NC Hills on four consecutive occasions upto 15 June 1992, which was due to expire on 12 December 1992.

According to the sub para (4) of paragraph 4, with the prior approval of the Governor Autonomous Council can established village and Court and make the procedure to be followed by the Court. In NC Hills no village court has been set up so far by the Council. But each and every tribe of the NC Hills has their own way for administering justice. These traditional have been approved by the Council.

Para 7(2) has empowered the Governor to make rules and procedure for the management of district fund. In this regard the NC Hills Autonomous Council framed rules with the prior approval of Governor which entered the statute book
as North Cachar Hills District Fund Rules 1953. According to Para 8(4), the Governor is the only competent authority to give assent to any bill passed by the Council for levy and collection of any taxes. Such taxes shall have no effect until and unless it is signed by the Governor. The following regulations have already been passed by the NC Hills Autonomous District Council so far.

1) The NC Hills Dist (Taxes) Regulation, 1953 and 1955
2) The NC Hills Dist (Revenue) Regulation, 1953
3) The NC Hills Dist (Taxes on entry of goods into Market) Regulation, 1959 and 1976
4) The NC Hills Dist (profession, trade, calling and employee) Regulation, 1972

Para 14(1) has authorised the Governor to appoint a commission at any time to examine on any matter relating to the administration of Autonomous Councils. In 2008 two Commissions were appointed by the Governor. The first was appointed to look into alleged financial anomalies of the NC Hills Autonomous Council and to proved nexus between NC Hills Autonomous Council and one militant outfit of the district. The second Commission is to enquire the recent bill passed by the 10th NC Hills Autonomous Council to change the nomenclature of the district.

There is a provision in the Sixth Schedule that in case of difficulty in the functioning of the District Council or difficulty for holding election in District Council, the Governor can take any action for the removal of such difficulty. In 2007, from 13 January 2007 to 10 December 2007, the North Cachar Hills Autonomous Council was under the control of the Governor due to unfavorable law and order situation to hold the 10th Autonomous Council Election. More recently in June this year, the Governor of Assam has taken over the administration of the North Cachar Hill Autonomous District Council after it was found that funds of the Council were diverted to a militant organization. This raises the question of accountability and proper use of funds made available for the ADC’s.

(c) The Khasi Hills Autonomous District Council of Meghalaya has put forward its views given below

In respect of exercise of discretionary powers of the Governor with regard to the Autonomous District Councils (ADC’s) and Autonomous Regional Councils (ARC’s), as provided under the Sixth Schedule of the Constitution of India, the
Governor is required to act on the basis of advice given by the Cabinet. Given below are the extract of the Gauhati High Court in this regard which is reported in AIR 1974 Gauhati 20.

"Paragraph 14 - Thus even if we assume that the powers exercisable by the Governor under the Sixth Schedule with regard to the Autonomous Districts and reasons are not in discharged of the executive functions of the State, but of the executive functions of the Governor. Such functions subject to the exceptions stated above must in view of Article 163 (1) of the Constitution of India, the exercise with the aid and advice of his Council of Ministers.

Paragraph 15- A question here arises for consideration. It is whether powers are conferred on a Governor in his personal capacity without reference to his Council, if the expression 'Governor' is used in any Article or provision in the Constitution. In our opinion, if the Governor has to act in his personal capacity whenever in any Article of the Constitution, the expression 'Governor' occurs. It will upset the whole Constitutional structure envisaged at the time when Constitution was passed and will make the Governor a kind of a dictator. To read every Article of the Constitution in which the expression 'Governor' occurs as conferring powers upon the Governor in his personal capacity without reference to the Cabinet would be constitutionally incorrect."

In view of the above, the Governor as per provisions of the Constitution is required to act on the advice of the Cabinet. The fall-out of this is that most of the Bills passed by the District Councils have to be routed through the State Government and as such they are yet to see the light of day or assented to by the Governor.

Further, on 11th February 1995 in exercise of his discretionary powers conferred under Clause (2) of paragraph 9 of the Sixth Schedule to the Constitution of India the Governor of Meghalaya has modified the existing ratio of 60:40 share of royalty of on coal between the Government of Meghalaya and the three District Councils fixed far back in the year 1956 by the Government of Assam to the ratio of 3:1 i.e. 75% to the State Government and 25% to the District Councils. This is an issue which has been taken up in another section of the Study.

(d) The Karbi Anglong Autonomous Council

The Governor of Assam has been provided with certain powers in regard to the administration of the autonomous areas. Any demarcation of changes in boundary of areas under the Sixth Schedule, or creation new council etc. have to notified by the Governor on recommendation of a commission appointed under sub para 1 of para 14 of the schedule.
As per para 16, the Governor can dissolve a District Council acting on the recommendation of the commission appointed under the para 14. Governor can also direct fresh election or assume the administration of the area himself subject to the fact that the District Council be given an opportunity of placing its views before the Legislature of the State. The Governor may also assume administration of District Council, as per the Assam Reorganization (Meghalaya) Act, 1969 even without any recommendation of a Commission, if he is satisfied that the administration is of the Autonomous District or Regional Council could not be carried on in accordance with the provisions of the Schedule. However such an order shall cease to operate after thirty days of the first sitting of the Legislature after the issue of the order, unless before the expiry of that period it has been approved by the Legislature as stated in the sub para (3).

The sub-para (2) of para 9 of the Sixth schedule requires that the any dispute over sharing of royalties accruing from licenses or leases granted for the purpose of prospecting or extraction-of minerals in respect of any area within the concerned Autonomous District, be referred to the Governor whose decision shall be final. It may be stated that this is the only para in the entire Sixth Schedule which still speaks of the Governor acting in his discretion in exercising power under the Schedule. The other specific provision was in para 18 which have been omitted by the North Eastern Areas (Re-organization) Act, 1971.

It has been seen that Governors also have the power to take over the administration of the ADC’s in case there is a constitutional breakdown of the machinery of the ADC’s. The intervention of the Governor of Assam in the case of the North Cachar hills Autonomous District Council has been noted in the case of Garo Hills Autonomous District Council, for instance, the Governors of erstwhile Assam and Meghalaya have taken over the administration of the Council as many as six times since its inception with the last instance from 16-04-2008 to 24-06-2008.

The Governor's role today has been mainly limited to giving his assent on the bills passed by ADC's after the advise of the State government concerned. There are complaints from almost all the ADC's that the process of approval of legislation is very slow and in several cases many bills have been kept pending for years. There is no doubt that the role of the Governor is very special in the context of the District and the Regional Councils and hence there is a need for Governors to be more involved in the ADC’s under their charge, be proactive to promote and facilitate local participative planning on Sixth Schedule areas. Further, the spirit of the Sixth Schedule is that the Governors are to function as the custodian of tribal autonomy and hence they should play a greater role in relation to the ADC’s and ARC’s. Proactive Governors can be very helpful in uplifting the deteriorating standards of administration and governance of the ADC’s.
B. An assessment of the exercise of the Judicial powers of the ADC's and ARC's as conferred under clauses 4 and 5 of the Sixth Schedule in the light of some illustrative case studies as also a study of the implications of the conflicts between State Law Enforcement Agencies and ADC's; Impact of 1953 justice Rules; and 1957 justice Rules.

The judiciary has been functioning in the desirous manner in some of the ADC's of the North Eastern Region. The powers of the judiciary are expressly defined under Paragraph 4 and 5 of the Sixth Schedule. Besides these the ADC's have their own set of justice rules such as the United Khasi-Jaintia Administration of Justice Rules of 1953 and the 1957 Justice Rules of the erstwhile Lushai Hills Autonomous District Council which is operative for three smaller Councils which were set up subsequently. All other ADC's have their separate set of Justice Rules. This being the situation a general assessment of the exercise of the judicial powers of the ADC's would not be very sustainable as the nature of judicial functions may differ from one ADC to that of another ADC. Hence we have to apply the case study method to get an understanding about the exercise of the judicial powers with some illustrative cases.

The North Cachar Hills Autonomous Council (NCHAC)

Paragraph 4th and 5th of the Sixth Schedule of the Constitution of India has provided judicial power to the Autonomous District Council. The NC Hills Autonomous Council framed The N C Hills Autonomous Dist (Administration of Justice) Rules 1955 and adopted three tier judicial system with Village Court at bottom, above that Subordinate District Council Court and District Council Court at the top. Despite having a provision for the establishment of Village Courts, this provision has not been put into operation in the North Cachar Hills. However, in every tribal village there is a traditional court and the Council has recognised these traditional village courts. Any appeal from the traditional court is referred to the Subordinate District Council Court.

The Subordinate District Court functions as original as well as an appellate court from the traditional village court. In the North Cachar Hills there is one sub-ordinate district Court which is situated at the head-quarter of Haflong. The Court exercises such powers as defined in the Chapter 3 of the Code of Criminal Procedure 1898. The number of judicial officers in the court is prescribed and appointed by the District Council with the prior approval of the Governor. All clerical staffs of the court are appointed by the Council. No Executive Member or CEM are eligible to hold the
office as Judicial Officer. The jurisdiction of the court has covered any cases arising within the North Cachar Hills.

Moreover, the Council can constitute an Additional Subordinate Court with the prior approval of the Governor of Assam. However, despite having this provision the Council has not been established any Additional Subordinate Court in NC Hills. The Council can also change the jurisdiction of any Subordinate Court within the Council.

The Subordinate District Council Court is not competent to try any suits in which one of the parties is a person not belonging to a schedule tribe and the offences fall under the section 124, 147 and 163 of the Indian Penal Code. Apart from that, without the prior approval of the Governor of Assam, the Subordinate District Council Court cannot be competent to try cases which is related to the sub-Para (1) of the para 5 of the Sixth Schedule to the Constitution of the India. If the Subordinate District Council Court was not specially empowered by the Governor, the court cannot be competent to try the cases which fall under the section 107, 108, 109,110, 144, 145 of the Code of Criminal Procedure of 1989.

At the top of the judicial structure there is District Council Court in the North Cachar Hills which is known as North Cachar Hills Autonomous Council Court. The number of Judicial Officers of the District Council Court is determined by the Council with the approval of the Governor. The appointment of the Judicial Officers of the court by the Council is also subject of the approval of the Governor. The court ordinarily sits at Haflong; however, there is provision to sit at any other place by the general or special order of the Council to settle any particular case. The court may act either on the report of the lower court or on the application of a party interested or on its own initiative.

In criminal cases the Subordinate District Court and the District Council Court try the case in the spirit of the Code of Criminal Procedure 1898. In case the person is residing out of the district or the person is belonging to non-tribal community the Court has to issue summon through Deputy Commissioner.

In all civil cases the District Court and Subordinate District Council adjudicate according to law, justice, equity and good conscience consistence with circumstances. If the District Council Court or Subordinate Court is satisfied that fraudulent disposal or concealment of property has taken place, the accused may be detained for the period not exceeding sixth months.
Whenever a village court has sentenced an offender to pay fine in a criminal case or has passed an order for the payment of money by person in a civil case the court can issue *parwana* for the payment of the amount by the offender of the person concerned. In such case the court may apply to the Chief Executive Member of the District Council to realise the amount of execution according to civil process against the movable and immovable property of defaulter. In the event of the non-recovery of the amount of execution, the Chief Executive Member of the Council can move the District Subordinate Court for arrest and detention of offender. Every warrant for the execution of sentence of imprisonment shall be directed through the Deputy Commissioner to the office in charges of the jail in which prisoner is to be confined. When the court issues warrant against any person who is absconding, any movable or immovable property of the offender is liable to be seized.

Since its inception the judicial system of the NC Hills has been maintaining peculiarity while judging the cases. The North Cachar Hills is the home of several tribes and every tribal society is guided by their own customs and traditions. They are still preserving their own traditional system for administering justice. Hence the judicial system of the District must have conformity with the traditional laws of every tribal community. The Judiciary of the North Cachar Hills, therefore, on several occasions has to dispose the cases on the basis of the customary law relating to each of the tribes inhabiting the district.

For instance we can cite one case which came for disposal before the Judge vide the case no 1/98 with Nolendra Hojai, second younger of late Devendra Hojai. The petitioner Jaithanon Hojai (adopted son of Devedra) alleged that Smt. Parbodi Hojai (Wife of the Dwijendra, first younger brother of Devendra) and her five sons captured all the land belonging to the late Devendra Hojai that used to be cultivated by Jaithanon every year. The court with a view maintaining proper justice and prevailing customary laws of the Dimasa Community decided the case, giving one gun, of late Devendra to his second younger brother Nolendra Hojai and the paddy field of the deceased was distributed between Jaithanon Hojai and Smt. Parbodi Hojai equally, i.e. 50:50.

In the above case the Court maintained the traditional system of the Dimasa tribe that the property like land, gun, house etc can be inherited only by the son of the family and not by any other person unless such properties are purchased or willingly given to the inheritors.
A case for the dissolution of marriage was also disposed by the Subordinate District Council on the basis of customary law. The case was brought by the Monjuly Syed of Jatinga village against her husband Sri Tyrshain Rymbai vide case no. 9/2009 and disposed on 16/6/2002. The Court heard both sides, but did not find any appropriate reasoning for dissolution of marriage. The court took the views and decision of the church and elders. All of them including mother of the plaintiff gave statement in favour of the dissolution of the marriage of the couple. However, the court by maintaining customary law of the Khasi Community barred to claim any movable and immovable properties of the wife and all three sons of the couple will remain with the mother.

Thus, there are many cases belonging to different tribes in North Cachar Hills where the court has given a judgment which are in conformity with the relevant tribal customary law.

The Karbi Anglong Autonomous Council

The Autonomous District Councils (K.A.A.D.C.) under the Sixth Schedule has provided certain judicial power as mentioned in the para 4th and 5th of the Schedule. As per power specified para 4, the Karbi Anglong Autonomous District Council is empowered to constitute “village councils or courts for trial of suits in which the parties are members of Scheduled Tribes other than those for which special provision has been made in Para 5.” Such village council or courts may “function to the exclusion of any court in the State” with the court constituted by the District Council as appellate authority. “No other court except the High Court and Supreme Court has any jurisdiction over the suits and cases triable by the village council or courts.” The K.A.A.D.C. has not constituted any village council or court. Recently the K.A.A.D.C. has adopted steps to establish district appellate court at Diphu and try matters related to customary laws. It is not known if any steps would be taken to constitute village council or courts. As per the para 5, the other cases are tried by the District Magistrate or any other designated officer.

The Council may constitute village councils or courts for the trial of suits and cases not being suits and cases of the nature referred to in the sub-para (1) of para 5 of this schedule, which the Governor may specify in this behalf, apply to the exclusion of any court in the state, and may appoint suitable person to be members of such village councils or presiding officers of such courts and may also appoint such officers as may be necessary for the administration of the laws made under para 3 of the schedule.
The Lai Autonomous District Council (LADC)

The Lai Autonomous District Council (LADC) had inherited the Pawi-Lakher Autonomous Region (Administration of Justice) Rules, 1954 and the same act was enforced till 1974. As the Judiciary is an important organ, signifying autonomous nature of the District Council system, adequate step was taken to improve the judicial system of L.A.D.C. As provided in Paragraph 4, sub-paragraph (4) of the Sixth Schedule to the Constitution of India, the L.A.D.C. (the erstwhile Pawi Autonomous District Council) had enacted the Pawi Autonomous District Council (Administration of Justice) Rules, 1974 with the approval of the then Lieutenant Governor of Mizoram. Accordingly, three tier courts, namely, Village Council Court, Intermediate District Council Court and District Council Court were created for the trial of suits and cases between the parties all of whom belong to Schedule Tribe or Tribes within the L.A.D.C. administered area. However, the courts have no jurisdiction to suits and cases to which provision in sub-paragraph (1) of paragraph 5 of the Sixth Schedule to the Constitution of India applies.

At present, there are 86 Village Council Courts in all the 86 villages where Village Councils are established, two Intermediate District Council Courts, which are located in Lawngtlai and Bualpui ‘Ng’, and the District Council Court, which is known as the Lai Autonomous District Council court or LADC Court, which is located at Lawngtlai. Thus the LADC has one District Council Court and two Intermediate District Council Courts and 86 Village Council Courts. The Village Council Court comprises of the President and a minimum of two other members. The quorum to constitute the sitting of a Village Council court shall extend to the hearing and trials of suits and cases arising within the territorial limit of the village. However, a Village Council court shall try suit and cases in which the parties belong to a schedule tribe or tribes’ resident within its jurisdiction. The Village Council Court can impose fine for any offence up to a limit of Rs. 60/- and may also award payments in restitution or compensation to the aggrieved or injured party in accordance with the customary law. Further, a Village Council Court also can impose a fine of up to Rs. 25/- upon a person who failed to attend the court as demanded by it. An appeal against the judgement of the Village Council Court can be initiated in the Intermediate District Council Court within sixty days of the judgement passed by the Village Council Court. The Intermediate District Council Court is presided over by Judicial Officer, appointed by the Executive Committee with the approval of the Governor and Court President and Recorder of the L.A.D.C. court. The Intermediate District Council court has original jurisdiction in all cases within its jurisdiction and cases referred to it by
Village Council courts. The Intermediate district Council court at Lawngtlai is looked after by the Revenue Officer (Headquarters) as Ex-officio Judicial Officer. Likewise, the parallel court at Bualpui ‘Ng’ is also looked after by the Revenue Officer posted there as Ex-Officio Judicial Officer. An appeal against judgement of the Intermediate District Council court shall lie to the L.A.D.C. Court and an appeal shall be initiated within sixty days of the judgement passed by the Intermediate District Council court. The L.A.D.C. court is the highest court in the L.A.D.C. administered area and it consists of three Judicial Officers, one of whom is appointed as the President and Recorder of the court by the District Council. Judgement of the L.A.D.C. Court should be delivered on the basis of majority opinion and any member of the District Council shall not be entitled to hold office as Judicial Officer. The L.A.D.C. Court has applied the Code of Criminal procedure 1898, Code of Civil Procedure 1908 and customary laws for delivering judgement on certain cases. It is a notable feature that the Court President and Recorder of the L.A.D.C. Court as well as Judicial Officers of the L.A.D.C. Court and Intermediate District Council Court are equivalent to Magistrate First Class of the State Government. As such, they can litigate and can try suits and cases up to the extend which can be tried by the First Class Magistrate of the state government. An appeal against judgement of the LADC Court can lie only in the Gauhati High Court and the limit for filling an appeal is ninety days from the date of order or decision, excluding the time for obtaining copy of order or decision. Up till now, no appeal has come up in the Gauhati High Court against the judgement of the L.A.D.C. court. Village Council Courts and Intermediate District Council Courts litigate many cases within their jurisdiction but only few cases came up to the L.A.D.C. court. L.A.D.C. has court tried 12 cases during the past one year and one appeal against the judgement of the Intermediate District Council Court was admitted in the L.A.D.C. court during the past one year.

The Autonomous District Councils of Meghalaya

Paragraph 4 and 5 of the Sixth Schedule provides for administration of justice in Autonomous areas. Under the above paragraphs, the ADC’s are empowered to constitute Courts for trials of cases between parties belonging to Scheduled Tribe communities. The District Council Court for each district consists of qualified Judicial Officers, designated as Judges and Magistrates who are appointed by the Executive Committee with the approval of the Governor under The United Khasi-Jaintia Hills Autonomous District (Administration of Justice) Rules, 1953 and the Garo Hills Autonomous District (Administration of Justice) Rules 1953.
Paragraph 5 of the Sixth Schedule provides conferment of powers on the District Council Courts suits or cases under the CPC and Cr. PC and these Courts have been exercising judicial authority, which have been of great service to the people, where delivery of justice is concerned.

The above mentioned courts try all cases at different level when litigation is within the tribal areas and party or parties involved are tribals. They disperse justice in line with the traditional customs and usages at a very speedy, simple and inexpensive manner. The Judicial Officers of the Courts of the District Councils function independently and free from interference by the Executive. Separation of the Judiciary from the Executive is in existence since the Constitution of the Courts in the Khasi and Jaintia Hills. The Garo Hills Autonomous District Council (GHADC) has till date not separated the Executive and the Judiciary. No doubt this has affected the functioning of both these wings of the GHADC.

The Judge and Additional Judge of the Courts of the Khasi Hills Autonomous District Council (KHADC) are conferred with powers for the trial of offences punishable with death and transportation for life under the Indian Penal Code or under any other law applicable. The District Council Courts are under the direct supervision by the Hon’ble High Court of Assam, Meghalaya etc.

The District Council stands for speedy, cheap and fair administration of justice to the people under its jurisdiction. The KHADC desires to have a legal aid cell to help and assist the poor litigants and ensuring free and fair justice to them. To bring about an efficient justice delivery system there is an urgent need to set up District Council Courts in Ri-Bhoi and West Khasi Hills District as well and to include all the Council Courts within the present e-Courts project/scheme.

In so far as Village Courts are concerned, they have been conferred with the power to try petty offences, but the said Courts are not empowered to convict and sentence a person for imprisonment, such other powers like awarding cost etc. are conferred upon such Court. In the same way District Council Courts are also been conferred with certain powers under Chapter III, Code of Criminal Procedure.

The District Council Court has been very active and has undertaken cases that had serious ramifications. In the case of State versus Shri. Phaster Kharbikhkiew, the accused, (G.R. Case No.17 (A) of 2004(U/S 302 I.P.C), the District Council Court had given life
imprisonment to the accused who was convicted of murdering Dimitrius Nengnong. The District Council Court’s verdict on Shri. Phaster Kharbhikhiew was not challenged in any higher Court of Appeal. The same court conducted hearings on the Fullmoon Dhar case related to the murder of two women. The position of the case is not certain as Fullmoon escaped from custody early this month and was killed by security forces during his pursuit.

Thus the above were some of the case studies of the judiciary in the various district Councils of the north eastern region. The judiciary has been found to be relatively active in almost all the District Councils other than that of the Tripura tribal Areas Autonomous District Council (TTAADC). The Judiciary under the TTAADC has never been functional since its inception. The Sixth Schedule provides the TTAADC to constitute Courts for the administration of justice involving indigenous tribal people, but so far there has been no move on the part of the TTAADC to make the Judiciary functional. Leaving aside Tripura it can be seen that the Judiciary has been vibrant in almost all the ADC’s. It has been very much independent in its functioning. The District Court in the K.H.A.D.C. has made it very clear that their ruling in matters of cases with grave importance has never been overruled by any higher Court.

The question regarding the conflicts between the State Law Enforcement Agencies and ADC’s does not arise as there has been a balance between the functions of the ADC’s and the State law enforcing agencies. The Study Group has found that the District Council Courts have to depend on the State Law Enforcement Agencies such as the Police, for use of the lock-ups, prisons for the under trial prisoners and those convicted. The State agencies also on their part have not encroached on the areas of jurisdiction of the Courts of the ADC’s. Though there have been constant clashes between the State governments and the ADC’s on various issues ranging from that of devolution of funds to various development works, but there has been rarely any dispute over that of the functioning of the Judiciary.
C. Role of the ADC’s and ARC’s in Planned Development and Identification of priority areas for capacity building for various functions

The core philosophy of the Sixth Schedule of the Constitution was aimed at the protection of the tribal people and their interests. Hence the ADC’s and the ARC’s were set up for various hill and plain areas of the North Eastern Region in 1952. These institutions are entrusted with the twin tasks of protecting tribal culture and customs and also undertake some development activities for the tribal areas. Therefore today it has become very important to get a clear perception about the role of the ADC’s and ARC’s in planned development. It was expected that the ADC’s would not only play an important role in protecting, preserving and promoting their respective cultures, but also play a vital role in the process of grass root development.

The Study Group has found that the different ADC’s have different structure and setup which has a direct bearing on the development process of such institutions. To talk about planned development without having a proper setup for the same in the ADC’s is like making a mockery of the entire concept of the process of planned development. The Study Group has found that some of the ADC’s do not have access to proper planning professionals. There are also no planning boards in the District Councils such as in the State of Meghalaya. Thus as of now, the process of development in some of the ADC’s is very negligible as they do not have the proper infrastructure to carry out such development activities.

The role of the ADC’s and ARC’s in the planned development and identification of priority areas for capacity building for various functions can be better understood with case studies of some States.

Lai Autonomous District Council

The Autonomous District Councils are authorized to receive funding from the State and Central Government in the form of grant-in-aid as enshrined in Article 275(1) of the Sixth Schedule to the Constitution of India. As such, the District Councils prepare their own budget that is sanctioned by the Central Government through the State Government in the form of grant-in-aid. The budget of the LADC is first passed in the LADC session, after which, it is sent to the Governor and the State Government for release of grant-in-aid. As enshrined in sub-paragraph (2) of paragraph 7 of the Sixth Schedule to the Constitution of India, the Mizoram Autonomous District Fund Rules, 1996 was framed.
by the Governor of Mizoram for management of the fund of Autonomous District Councils of Mizoram. So, grant-in-aid received from the Central Government through the state government is deposited in the District Council fund, which is also known as LADC Fund. Further, taxes and other revenues that are levied under the laws, rules or regulations framed by the LADC under paragraphs 3, 4, 6, 8, 9 and 10 of the Sixth Schedule to the Constitution of India are deposited in the LADC Fund. Thus, all funds received by the LADC whether it is grant-in-aid from the Central Government, various central funding projects and revenue receipt of the LADC are deposited in the LADC Fund.

The LADC has a Planning Department which is administratively headed by the Planning & Development Officer (P&DO.) and Assistant Planning & Development Officer (A.P & D.O.). The Chief Executive Member (CEM) is the ex-officio Chairman of Planning Board in LADC whose position is similar to the Chief Minister as Ex-Officio Chairman of the State Planning Board. In like manner Vice Chairman, State Planning Board is appointed by the Chief Minister with the approval of the Governor, the CEM also appoints the Vice Chairman, Planning of LADC (with the approval of the Governor of the State. In fact, policies, programmes and plans are formulated by the Vice Chairman as head of the Planning Board that is implemented and pursued by the P&DO. as administrative head. The budget for financial year of LADC is also planned and prepared by the P&D.O. and his staff. This is tabled in the LADC session, and budget is prepared as enshrined in Paragraph 13 of the Sixth Schedule to the Constitution of India. After the budget is adopted and passed by the legislature of LADC, it is sent to the Governor for his approval. After being approved by the Governor, the estimated budget money is sanctioned by the Government of India in the form of grant-in-aid through the Government of Mizoram.

In this way, plan budget has been prepared by the LADC to enable it to perform development work for its administered area by including various priority subjects in the budget.

However, the Government of Mizoram has negated the budget prepared and passed by the LADC many a time in the past. Not only the LADC, all the ADC's of Mizoram were instructed by the State Government to prepare their budget within a specified limit in the past. Due to that, complaints were often raised by the ADC's due to the restriction imposed by the State Government. The District Councils are quite hopeful that the present Government of Mizoram will be generous in fulfilling their (District Council) aspiration with respect to funding and financial assistance. As such, the present government of LADC is also quite hopeful of ensuring good development work in its area with the new
liberal policy of the government of Mizoram. Therefore, time will tell whether the new
development will concretize into real development of the area.

It should be recollected that the first budget of the LADC in the form of grant-in-aid
from the Central Government and state government was Rs. 7.50 Lakhs in 1972-1973,
which increased to Rs. 2000 Lakhs in 2001-2002. And, the budget of LADC in the past
year i.e. 2008-2009 was Rs.3023.60 Lakhs. The State government in different phases
released the funds of the LADC and the Deputy Commissioner of Lawngtlai District on
behalf of the Government of Mizoram also countersigns utilization certificate of the
fund. Besides the annual financial budget which is released in the form of grant-in-aid,
various Central funding schemes known as Rashtriya Sam Vikash Yojana (RSVY),
Backward Region Grant Fund (BRGF) and other centrally sponsored funds are also allocated
to the LADC for implementation of development work.

North Cachar Hills Autonomous District Council

One branch of the North Cachar Hills Autonomous District Council Secretariat is headed
by a Principal Secretary who is an IAS or Assam Civil Service officer assisted by the other
secretaries and officers deputed by the State Government of Assam. Paragraph 6(2) of
the Sixth Schedule to the Constitution of India provides the State Government to transfer
certain departments to the District Council and accordingly the State Government of
Assam has entrusted 14 and 30 departments in the year 1970, and 1995 respectively to
the District Council. For the purpose of administering these departments the secretariat
was created. All the officers and the staff of these departments are State Government
employees placed under the disposal of the Council.

In 1970, for the first time, in exercise of power conferred under the paragraph 6 (2) of the
Sixth Schedule, the State government entrusted (no TAD/R/153/70) the executive
function of the State to the NC Hills Autonomous Council in respect of 14 subjects. All
the plan and non plan schemes relating to these subjects had been transferred to the
District Council on 1st June, 1970. These 14 subjects are:

1) Agriculture
2) Minor irrigation
3) Soil Conservation
4) Animal Husbandry
5) Dairy and Milk  
6) General Education including Cultural programme  
7) Forest  
8) Fishery  
9) Road and Building  
10) Water Supply  
11) Health and family planning  
12) Social Welfare  
13) Cottage industries  
14) Community Development Programme  

The State Government had also prescribed the terms and conditions for the entrustment of these 14 subjects to the Council. While executing the schemes under these entrusted subjects the Council has to abide by these terms and conditions laid by the State Government.

Under the same terms and conditions in 1976, the State Government of Assam entrusted several functions to the NC Hills Autonomous Council along with Karbi Anglong Autonomous Council in relation to co-operation. Both the plan and non plan schemes relating to this subject are transferred to NC Hills. Accordingly the following schemes had been entrusted to the NC Hills District Council under the co-operation department:

1) Agriculture plan schemes  
2) Processing other than factories and other large processing unit  
3) Marketing  
4) Farming (Agriculture and non-agriculture  
5) Consumable  
6) Industries  
7) Forest labour Co-operative  
8) Handloom development Schemes  

However, the people of the two hills districts were not satisfied with the conditions for
the entrustment of power to the District Council by the notification TAD/R/153/70 of Assam govt. As a result, a demand for changing these conditions has been made often by the NC Hill and Karbi Anglong District Councils. Responding to the perpetual demands from the two Autonomous Districts, the Assam Government set up a Committee to examine the matter and finally with the recommendation of the Committee the Assam Government revised some of them.

For the purpose of the administration of these entrusted departments a separate secretariat was created with the Principal Secretary and other secretaries deputed from the State Government. In 1996 the Council was further entrusted 30 Departments. These were:

1) Industry
2) PWD
3) Sericulture
4) Animal Husbandry and Veterinary.
5) PHE
6) Forest
7) Agriculture
8) Education:
   a) primary Education up to the level of Higher Secondary Education;
   b) Adult Education
9) Cultural Affairs
10) Co-operation
11) Fisheries
12) Panchayat and Rural development including DRDA
13) Handloom and Textile
14) Health and family welfare
15) Irrigation
16) Social Welfare
17) Weight and Measure
18) Food’s Civil Supplies
19) Town and Country Planning
20) College Education (General) including Library service, District Museum, Archaeology
21) Sports and Youth Welfare
22) Soil Conservation
23) Land Reform
24) Public Relation
25) Tourism
26) Excise
27) Transport
28) Printing and Stationary
29) Flood Control Department
30) Finance Including sales tax on purchase of Goods other than News papers, professional tax.

As per amendment of the Sixth Schedule in 1995, 15 departments have been brought under a new paragraph 3 (A). For these Departments the Council can make laws. State Government laws and executive powers do not extend to these departments. However, the Council has not made any law under Paragraph 3 (A). Thus virtually, executive power of the Autonomous Council extended to all the Government Departments except a very few that remain under the State Government.

**Autonomous District Councils in Meghalaya**

The study of the Autonomous District Councils in the State of Meghalaya presents a totally different picture when we compare it with the ADC’s of other states in the North Eastern Region of India. The ADC’s of Meghalaya are not equipped with any infrastructure to deal with planned development. The idea of Planning Board within the District Councils also does not exist. The ADC’s do not have any access to any planning professionals who can lend their expert advice in the planning process.
The Study Group on its visits to the District Councils of Meghalaya and interaction with the Members of the ADC and officers of the ADC’s found out that even after more than fifty years of their existence, the ADC’s of Meghalaya have put little emphasis on the concept of planned development. The three Autonomous District Councils of Meghalaya are under the Constitution of India under Article 271(1), provided funds from the Consolidated Fund of India to the ADC’s. The three ADC’s are also recipients of funds under the 11th and the 12th Finance Commissions. But the funds provided are too inadequate to have much impact in the social, economic and the physical developmental initiatives of the Councils.

The ADC’s of Meghalaya point out that it cannot carry out the process of planned development in a manner desired by the people because the District Councils are under the control of the State Government vide Paragraph 12(a) of the Sixth Schedule and hence they have to depend on the decisions of the State Government for the allocation of the resources. The ADC’s also point out the lack of the financial resources as a major factor that hinders the District Councils to carry out development process. The ADC’s have pointed out that the exemption of Meghalaya from the 73rd Amendment has debarred the State from the benefits of Direct Funding from the Panchayati Raj Ministry and other Central Government institutions. The problem is that even if the Central Government agrees for direct funding, the District Councils do not have the necessary infrastructure to carry out the process of planned development.

The ADC’s in the State of Meghalaya have never been able to carry out development activities in a systematic manner mainly because the State Government does not want it to play an important role in such regard. The fact that there has never been any major amendment to increase the powers of the ADC’s shows the lack of interest of the State Government in this regard. Perhaps it is an irony that the ADC’s of Meghalaya are the only ones that have remain stagnated with the same amount of powers and functions since their inception in 1952. There is no doubt that the ADC’s of Meghalaya can play an important role in the process of development, but for that to happen, there has to be a major overhaul in the powers and functions of the District Councils of Meghalaya and also that the State Government has to change its present approach of seemingly neglect towards the District Councils and make it a co-partner in the process of development. There have been too much talk and little action in this regard. There has to be a re-look at the entire setup of the ADC’s in the state of Meghalaya. The ADC’s in collaboration with the traditional local self-governing
institutions, if empowered, can play a vital role in carrying out planned development at the grass root level.

**Bodoland Territorial Council**

The Bodoland Territorial Council has the most impressive setup of infrastructure among all the District Councils of the North East. Fund and development package of BTC as of present is very sound. Both Central and State governments provide Rs.100 Crores per annum for 5 years. There is also ‘one time financial assistance’ for the development of administrative infrastructure such as BTC Secretariat at Kokrajhar, new District Headquarters, Sub-Divisional Headquarters and Block Headquarters.

The State Government also offers possible and sustainable additional incentives for attracting private investment in the Council area and also supports projects for external funding.

It has also been mentioned in the MOS that a centrally funded Central Institute of Technology (CIT) will be set up to impart education in various technological/ Vocational disciplines such as Information Technology, Biotechnology, Food Processing, Rural Industries, and Business Management etc. It also further mentioned that (CIT) will be upgraded to a centrally funded State University with technical and non-technical disciplines to be run by the BTC.

But for continuous fund flow resource mobilization through imposition of taxes is necessary. The BTC authority can levy and collect taxes on lands and buildings, professions, trades, employments, on animals, vehicles and boats, on entry of goods into a market for sale there in, on tolls passengers and goods carried.

List of subjects entrusted to the BTC

1. Small, Cottage and Rural Industry
2. Animal Husbandry & Veterinary
3. Forests
4. Agriculture
5. PWD
6. Sericulture
7. Education
   (a) Primary Education
   (b) Higher Secondary including vocational training
   (c) Adult education
   (d) College Education (General)

8. Cultural Affairs

9. Soil Conservation

10. Co-operation

11. Fisheries

12. Panchayat and Rural Development

13. Handloom and Textile

14. Health and family Welfare

15. Public Health Engineering

16. Irrigation

17. Social Welfare

18. Flood Control

19. Sports and Youth Welfare

20. Weight and Measures

21. Library Service

22. Museum & Archaeology


24. Tribal Research institute

25. Land and Revenue

26. Publicity & Public Relation

27. Printing and Stationary

28. Tourism
29. Transport
30. Planning and Development
31. Municipal Corporation, Improvement Trust, District Boards and other local authorities
32. Welfare of Plain Tribes and Backward Classes
33. Markets and fairs
34. Lotteries, Theatres, Dramatic performance and Cinemas
35. Statistics
36. Food and Civil supply
37. Intoxicating liquors, Opium and Derivatives etc
38. Labour and employment
39. Relief and Rehabilitation
40. Registration of Birth and Deaths.

The above powers and functions given by the Government of Assam to the BTC make it amply clear that the State Government wants the District Council to play a vital role in the process of development. The BTC has separate departments to deal with developmental issues and it has been able to implement some of its major development projects in a smooth manner.

**Tripura Tribal Areas Autonomous District Council**

**ADMINISTRATIVE SET UP:-**

The Council administration is headed by the Chief Executive Officer, normally an IAS officer, assisted by an Additional Chief Executive Officer and Dy. Chief Executive Officer, and Executive Officer who are normally from the State Civil Services. The principal officer acts as the departmental heads for the different departments like animal husbandry, fishery, forest, education, cooperation, health, industry, land records and settlements, Panchayat, publicity and welfare. The PWD is looked after by the Superintendent Engineer along with Executive Engineers. There are four Zonal Development Offices viz:- Khumulwng(H.Q. West Tripura District) Birchandra Manu(South Tripura District) Gandha Charra (Dhalai District) and Manu Ghat (Dhalai District). The Zonal Development Officers
look after the Zonal offices. There are also 37 Sub-Zonal Development Officers looked after by the Sub-Zonal development Officers for the implementation of the different schemes of the TTAADC. To coordinate the planning work there is a planning cell looked after by a Sr. Research Officer deputed by the State Government.

BRIEF ACTIVITIES OF THE VARIOUS DEPARTMENTS

1. AGRICULTURE:-

Agriculture is the main occupation of the people living within the TTAADC area. The agriculture wing of the TTAADC is also looking after horticulture, soil and water conservation and development of market schemes. Some of the schemes implemented by the dept. are as follows:-

(a) Conducting of different demonstration and supply of seeds.
(b) Demonstration and training programme of vegetable in compact areas.
(c) Jhum and upland cultivation.
(d) Market development programme.
(e) Providing of agricultural implements on subsidy such as power tillers, sprayers, pushcarts etc. to the poor farmers.
(f) Providing of plant protection services by making sprayers on rent and free plant protection chemicals.
(g) Development of Human Resource by training of staff and the farmers.
(h) Demonstration on horticultural crops for utilization on the dry land.
(i) Encourage vegetable growth by providing improved and high yielding varieties seeds.
(j) Market development for the sale of the produce of the poor farmers.
(k) Self employment through horticulture.

1. Soil and water conservation.

2. WELFARE DEPARTMENT:-

Large sections of the population within the TTAADC area are ‘Huk’ or shifting cultivators and landless tribal. Additional economic emphasis is provided for their upliftment and improvement of their socio-economic conditions. The District
Council has adopted the following scheme for providing financial assistance to 26,000 families every year on wage basis per man day per family. The scheme includes distribution of 20 kgs. Paddy seeds per family to the shifting cultivators. The following schemes are also implemented with a view to extend financial help to the poor and deserving tribal:-

(a) Housing scheme for construction of house Rs. 20,000/-
(b) Assistance of business Rs. 5,000/- each for hawker and Rs. 7,000/- each for shopkeeper.
(c) Integrated Jhumia Resettlement Scheme through rubber plantation.
(d) Construction of tribal rest house.
(e) Nucleus budget scheme.
(f) Special incentive for tribal areas.
(g) Implementation of rubber plantation for jhumia families.

3. BORDER AREA DEVELOPMENT PROGRAMME:-
Different schemes have been taken up under this programme for the development of inaccessible hamlets along the international Indo-Bangla border area. The total number of beneficiaries is 4897 families. The scheme of the program includes creation of community assets in the form of: - (i) Link road (ii) drinking water facilities (iii) mixed crop/ upland paddy cultivation (iv) Construction of 50 seated hostel for boys and girls and individual benefit scheme are (i) Housing scheme for construction and renovation (ii) Supply of seedlings (iii) Rubber plantation (iv) Distribution of household goods etc.

4. INDUSTRIES:-
The policy of the TTAADC is to develop small and cottage industries including other agri based industries like sericulture. There are 53 nos. of industrial training centres under the different trades like weaving, cane and bamboo, tailoring, bee-keeping, carpentry etc. The District Council also distributes yarn free of cost to the selected distressed tribal women weavers. Assistance is also given to rural artisans especially to those who have been trained but unable to purchase tools and equipments to start their own business and profession.
5. INFORMATION, CULTURAL AFFAIRS, YOUTH PROGRAMME AND SPORTS:-

The department is playing a vital role to highlight the activities and developmental works undertaken by the Council. It publishes a literary magazine *Khumulwng*. A tribal cultural academy has been set up in order to extend opportunities for cultural activities among the tribal. Distribution of free modern musical instruments along with organizational of musical and folk song competitions are undertaken besides traditional fairs. The department also distributes sports goods free of cost to different clubs and organized rural sports and games.

6. HEALTH:-

The health department with limited resources is doing its best to keep up the slogan of the World Health Organization “HEALTH FOR ALL BY 2000 AD”. The poor tribal patients are benefited as they get checkup and the required medicine free of cost. During the period 2000-2001, 16,134 patients and 2001-2002, 18,192 patients were benefited under the scheme. Health camps are also conducted in the fur flung remote villages where medical facilities are not available. During the period 2000-2001, 122 camps and 2001-2002, 106 health camps were conducted.

A mini 20 bedded Kharengbar hospital is also functioning at Khumulwng, HQ of the TTAADC. The hospital is looked after by 3 Medical Officer. There is also a Homeopathic dispensary looked after by a qualified physician. During the period 2001-2002, 15897 patients, 2005-06, 7614 patients and 2006-07, 7011 patients were treated and given free medicines. Apart from that health camps were held in the interior far flung villages. During 2005-06 there were 18 health camps conducted and 4414 patients were treated and 2006-07, 16 health camps were conducted and 2829 patients were treated. In order to meet the growing demands of health care, Voluntary Health Guide scheme has been introduced. The objectives of this scheme are to provide basic training to the unemployed youths on health care, first aid and knowledge on some of the common diseases prevalent in the rural areas and to distribute medicines to the patients free of cost for controlling the outbreak of seasonal diseases.

7. FISHERIES:-

Seeing the potentialities of fish farming, various fisheries programme have been undertaken to alleviate the economic condition of the rural tribal. Some schemes were implemented during the year 2005-2007 like infrastructure development, integrated pisciculture and production of fish and fish seeds. About 400 Jhumia
families (shifting cultivators) were motivated and rehabilitated with the fisheries program. Besides this semi-intensive fish culture has been taken up in six cluster villages. The scheme of the dept. includes construction and repair of mini barrage and pond, supply of various types of nets, boats etc. The department also distributed fish fingerlings free of cost to the farmers. Selected beneficiaries were imparted training on fish production, improved method of fish cultivation and control of diseases etc.

8. PUBLIC WORKS DEPARTMENT:-

The Public Works Department of the TTAADC has four working division and each division is co-terminous with zones of the Sixth Schedule area and revenue district of the state, excluding panchayat areas. The office of the Northern Division is located at Pecharthal, Dhalai Division at Ambassa, Southern Division at Birchandra Manu and Western Division at Khumulwng. The department looks after the construction of various types of building work, rural water supply, communication, irrigation and assist in the work of rural electrification. Under the rural water supply scheme special program have been taken up for ensuring safe drinking water facilities to the people in general and the hilly region in particular. It is pertinent to mention here that most of the areas under the council area are covered with high hills. Minor irrigation scheme is also going on to bring more agricultural lands under cultivation. Communication is a hindrance for the development of the TTAADC. The area under the district council being hilly, there are many streams, rivulets, rivers etc. It is because of this reason that more stress have been given to construct new road, foot tract, culverts, bridges etc. for ensuring easy communication. Constructions of various building works have been going on for a long time and many of them have been completed already.

9. RURAL DEVELOPMENT:

The main objective of the Scheme of rural development is generation of employment amongst poor people living in the rural areas. In short it tries to eliminate poverty in the rural areas. Schemes like Training of Rural Youth for Self Employment (TRYSEM) in different trades like motor driving, stenography etc. are being taken up. Safe and clean drinking water in rural areas through construction of sanitary ring wells and installation of Mark-II & III are also being undertaken.
10. VILLAGE DEVELOPMENT COMMITTEE

TTAADC’s major achievement during the period 2005-2007 has been the election of local bodies at Village level and the constitution of elected village committee in February 2006. These village committees derive their power and responsibilities under section 20 and 21 of TTAADC (Establishment of Village Committee) Act 1994. The power and duties include the implementation of the development schemes of the Council, State government and the Central Government relating to selection of beneficiaries/sites of projects, monitoring and supervision of such scheme/program in the village level.

Thus, the various departments in the TTAADC are working for the overall development of the district council. However, impacts of such activities are yet to percolate among the downtrodden masses. It is also a fact that the TTAADC have not been able to fulfill the aspirations of the indigenous people of the State for it has been established. Let us see some of the reasons as to why the TTAADC is not able to fulfill the aspirations of the indigenous tribal people:

The powers and functions of the TTAADC are not well equipped to deal with the kind of aims and objectives set before it. There is a gap between the powers and functions of the TTAADC and the aspirations of the indigenous people. The present movement for more autonomy to the TTAADC itself speaks for its own. It is pertinent to mention here that earlier it was thought that the powers and functions of the TTAADC were sufficient enough to deal with the purpose for which it has been established. But as time passed by it has been realized by the indigenous people that until and unless more autonomy in the form of functioning and finance is given, the TTAADC can not function. So, there are now demands from various corners, political and non-political for more autonomy for the District Council, even up-grade it to the extent of a separate state.

The success of the Autonomous District Councils fulfilling in their developmental role depends crucially on their capacity to design and implement plans. But the Study Group has found that almost all the councils do not have access to proper planning professionals. There is also no specialized setup within the councils for planning. This results in short term thinking on development, leading to an ad-hoc conception of development projects without proper technical and financial considerations. Therefore, there has to be an attempt to build capacity development for planning, monitoring and evaluation of the various projects at the District Council level.
D. Areas of enhancement of autonomy in the light of 73\textsuperscript{rd} and 74\textsuperscript{th} Amendments and some features of Panchayati Raj Extension to Scheduled Areas (PESA), 1996. (The reference is to some features of P.E.S.A., which is otherwise applicable to Fifth Scheduled Areas, with express objective of enhancement of autonomy for ADC’s and ARC’c in Sixth Scheduled Areas.

The case of enhancement of autonomy of the already ‘autonomous’ district councils is debatable. The fact that there is an attempt to enhance the autonomy of ADC’s shows that there is apparently something wrong in the entire setup of the ADC’s. The ADC’s have been trying to play an important role with limited autonomy and hence, there is a need to enhance the autonomy of some ADC’s in the North Eastern Region. One has to understand that not all ADC’s are weak, and that for those ADC’s that are weak, constitutionally, their autonomy has to be enhanced. There is a very interesting aspect is that almost all the ADC’s, if compared, have glaring disparities in their powers and functions and area of jurisdiction, although all of the ADC’s and ARC’c fall under the same Sixth Schedule. Here again we have to make a distinction between the ADC’s that originally came along with the Sixth Schedule in 1952 and the ADC’s that were created later to satisfy the aspirations of certain groups of people.

The ADC’s that came along with the Sixth Schedule were the United Khasi – Jaintia Hills Autonomous District Council (later it was bifurcated into two districts viz, the Khasi Hills Autonomous District Council and the Jaintia Hills Autonomous District Council in 1964);

the Garo Hills Autonomous District Council;

the Lushai Hills Autonomous District Council;

the North Cachar Hills Autonomous District Council;

the Mikir Hills (now Karbi Anglong) Autonomous District Council.

The above mentioned were the District Councils which came up in 1952 and which continue to operate today with the exception of the Lushai Hills District Council which was abolished after the formation of the Union Territory of Mizoram. Besides these original District Councils, there are many other District Councils which have been established largely are a response to conflict solution measure and also to satisfy the protectionist and development urge of certain communities.
The Autonomous District Councils that came into existence in 1952, especially that of Khasi, Jaintia and Garo Hills have been having more or less the same powers and functions that are spelt out in the original Sixth Schedule and has almost remained static to the present day.

The District Councils that were created later, such as the Bodoland Territorial Council, and the Tripura Tribal Autonomous District Council have been entrusted with powers and functions that are much more than the other ADC’s. Even the Autonomous District Councils of the Maras and the Chakmas in Mizoram have more powers and functions at their disposal than the ADC’s of Meghalaya. Thus leaving aside Meghalaya, the other States with the ADC’s and ARC’s have brought some amendments and added more powers and functions to the ADC’s which has certainly enhanced their autonomy.

The question of comparing the ADC’s with the Panchayati Raj structure to upgrade the autonomy of ADC’s and ARC’s is not that viable as both the institutions, those under the Sixth Schedule and Panchayati Raj are totally different in their way of style and functioning. The 73rd and 74th Amendments and P.E.S.A are instruments which are related to local self-governance and hence should not be compared with ADC’s and ARC’s. It has to be kept in mind that the Panchayati Raj structure was aimed at grassroot level democracy, whereas ADC’s and ARC’s are different in their nature and functioning. Panchayati Raj system with the 73rd and 74th Amendments is a very simplified model of local self-governance at the grassroot level with a greater degree of participation. The Panchayati Raj system is also meant for a greater amount of development at the grassroot level for which they have been effectively provided with powers and functions at various levels. The ADC’s and ARC’s are not the same as Panchayati Raj structure, but have a different meaning. The ADC’s were originally not even looked at as agencies for decentralisation of powers, although at a later stage some of the ADC’s were devolved with substantial amount of powers and functions. Thus the Study team is of the opinion that to equate ADC’s with Panchayati Raj institutions would not be fair to the ADC’s.

The Study Group after having had a detailed study of the features of P.E.S.A. and the 73rd and 74th Amendments is of the view that the features of P.E.S.A. are not much relevant in terms of enhancement of autonomy in areas under the ADC’s and ARC’s. Should a careful analysis be made it may become clear that some of the ADC’s are more powerful than that of Panchayati Raj institutions. For instance, the Bodoland Territorial Council of Assam has much more powers and functions than the Panchayati Raj institutions.
The implementation of the 73rd and 74th Amendments have been a watershed in enhancing grass root level democracy in India. These amendments have changed the entire face of democratic decentralisation and local level participation in the process of development at the grassroot level. Many of the provisions of the 73rd and 74th Amendments were excellently drafted such as reservation of seats for women, holding of election every five years, making Panchayati Raj bodies financially viable and involving them in micro-level planning with the suggested list of 29 subjects in the Eleventh Schedule for Panchayats, one can say that the local bodies at the district level and below have become the third tier of governance in the Indian federal structure. Article 243 (G) defines Panchayats as institutions of local – self governance. It implies that they must have the autonomy and power to govern in an exclusive area of jurisdiction.

It should be remembered that ADC’s were not seen as institutions of local – self governments, as were/are the Panchayats. ADC’s have different meanings and functions and are obviously different from the Panchayati Raj structure. ADC’s in the North Eastern Region except that of Meghalaya, have more or less sufficient powers and functions and hence there is very little that can be taken from the 73rd and 74th Amendments and the P.E.S.A. of 1996 and applied to the ADC’s for the enhancement of autonomy in the Sixth Schedule areas of North-East India.

The Study group has learnt that the quantum of autonomy to the various ADC’s barring that of Meghalaya has been increased from time to time. For instance, the Karbi Anglong Accord dated 1 April 1995 signed between the Government of India, Government of Assam and the Tribal bodies of Karbi Anglong and North Cachar Hills, drastically increased the powers and functions of the ADC’s by transferring 30 additional departments to the Karbi Anglong Autonomous District Council and the North Cachar Hills Autonomous Council, thereby enhancing their autonomy. The only ADC’s whose autonomy has not been reviewed are that of the state of Meghalaya. The Government of India Government of Meghalaya perhaps in their own wisdom did not feel the need to enhance the powers and functions of the ADC’s in the State Meghalaya. There appears to be some concern by the ADC’s in Meghalaya that their powers have not been enhanced. However, there appears to be no move from the ADC’s and the State government to take any steps in this regard.

On the whole Study Group is of the view that the enhancement of autonomy of the ADC’s of North Eastern Region has to be tackled from different perspective and not merely by bringing some of the features of 73rd and 74th Amendments and P.E.S.A. to the ADC’s and ARC’s.
The Study Group is of the opinion that the one important feature that can be taken out of the 73rd and 74th Amendment is that of the constitution of a Finance Commission by the Governor every five years to maintain the financial position of the ADC’s and thereby recommend suitable measures which many enhance the financial stability of the ADC’s. The Governor may also direct the ADC’s to be more transparent and accountable in their financial matters. Another pointer for the enhancement of the powers of the ADC’s with the functioning of the Panchayati Raj institutions is that there should be reservation of seats for women and positions in all ADC’s. As these Councils receive grants from Government, amendment may be introduced in the Sixth Schedule to provide for greater representation of women in the functioning of these Councils. This may be provided despite resistance to such change by some traditional institutions. The run up to the recent elections in the State of Meghalaya saw a member of women standing for elections. This is an indication that women are getting interested in competing for representation in the Councils.

The autonomy of the ADC’s and AR’s has been threatened by various factors, one of them being the State government itself. Hence the enhancement of autonomy for the ADC’s has to be looked from a different perspective. The most important factor that hinders the autonomy of such institutions is that of finance. The ADC’s have to depend on their respective State governments for their finances in the form of grants-in-aid. The State governments on their part invariably delay the issue of grants in aid to the ADC’s, thereby making the latter to depend on the Government. Making the ADC’s financially viable/sound through the Central grant would go a long way in enhancing their autonomy. The question of direct funding to the ADC’s by the Central Government may be considered and in response to this new development, and if granted, the ADC’s must show greater responsibility in becoming more transparent and accountable in their financial matters.

The other aspect which hinders the autonomy of the ADC’s particularly of the State of Meghalaya is that of legislation. In the case of Meghalaya, the State legislature has the power to override the decision of the ADC’s vide Paragraph 12A of the Sixth Schedule. When the State of Meghalaya was formed, a new paragraph (paragraph 12A) was inserted in the Sixth Schedule. It states that:

“Notwithstanding anything in this Constitution, if any provision of a law made by a District Council in the state of Meghalaya with respect to any matter specified in sub-paragraph (1) of paragraph 3 of the Schedule or if any provision of any regulation made

\[\text{[Paragraph 12A]}\]
by a District Council... in the state under para 8 or para 10 of the Schedule, is repugnant to any provision of a law made by the legislature of the state of Meghalaya with respect to that matter, then the law or regulation made by the District Council or as the case may be,... whether made before or after or after the law made by the legislature of the state of Meghalaya, shall to the extent of repugnancy, be void and the law made by the legislature of the state of Meghalaya shall prevail”.

Paragraph 12A empowers the laws of the State government to over-ride the laws passed by the ADC’s ‘even in matters allotted to the District Council by the Constitution of the Country’. To bring some amount of autonomy to the ADC’s of Meghalaya, this paragraph 12A may perhaps be modified to bring a balance in the relationship between the ADC’s and the State legislature.

The Study Group after analyzing the reports of various ADC’s has found out that the District Councils were either not interested in enhancing their existing position with some of the provisions provided in P.E.S.A or had no opinion on the matter. Two District Councils of Meghalaya have given some ideas in relation to P.E.S.A. According to the K.H.A.D.C the imposition of the provisions of Panchayati Raj system in the state is uncalled for and will be resisted by the Council. This view is further enforced by the fact that Meghalaya has been intentionally exempted from the purview of the 73rd Amendment. This means that there is a belief in the Centre of the distinct possibility and scope for further strengthening of the existing traditional grass root institutions of Meghalaya so as to bring them at par with the Panchayats. The K.H.A.D.C believes that there is no need to bring in any provision of the P.E.S.A. in the State and that the need is to strengthen the existing system through relevant legislations. On the other hand the Garo Hills Autonomous District Council has seen the possibility of applying some aspects of the Panchayati Raj institutions and has made an amendment to one of its legislations to make provision for the application of P.E.S.A.
E. Common Minimum Consistency and Parity (CPMP) in the function / responsibilities, assigning of functionaries, and devolution of funds, mobilization of resources through levy of taxes etc, and mode of fund flow.

The Sixth Schedule to the Constitution of India provides for the creation of ADC’s and ARC’s in some of the states of the North Eastern region. The ADC’s draws its strength from the Sixth Schedule and when the ADC’s were originally created in 1952, they had more or less the same amount of powers and function. However, as years passed by there were demands for more ADC’s by various tribes. Today there are ten ADC’s in the North Eastern Region under the Sixth Schedule. Though all the ADC’s fall under the Sixth Schedule they differ from each other in terms of their powers and functions. Thus there is very little common minimum consistency and parity in the functions/ responsibilities, assigning of functionaries, and devolution of funds, including mobilization of resources through levy of taxes etc, and mode of fund flow among the various Autonomous District Councils.

The most important reason behind the variance in the powers and functions of the ADC’s is that the powers and functions of almost every ADC’s has been increased and modified according to the requirements of different ADC’s. The only ADC’s whose powers and functions have remained static since their inception are that of the Khasi Hills Autonomous District Council (KHADC), Jaintia Hills Autonomous District Council (JHADC) and Garo Hills Autonomous District Council (GHADC) in the state of Meghalaya. Some powers and functions are almost the same for every ADC, and these are provided by the Sixth Schedule itself through Paragraphs III, IV, V, VI, VII, IX and X.

The Sixth Schedule had initially provided for equal powers and functions for the ADC’s of:

(i) the Garo Hills
(ii) the United Khasi-Jaintia Hills
(iii) the Lushai Hills
(iv) the Mikir Hills (now Karbi Anglong)
(v) the North Cachar hills.
The above were the District Councils that at the time of its inception had same amount of powers and function provided by the Sixth Schedule. But subsequently there were more ADC’s for various tribes of the North Eastern Region. Though all the ADC’s derive their strength from the Sixth Schedule, but the fact is that in time the ADC’s have different powers and functions assigned to them. This is largely because ADC’s have different needs and this has been appreciated by some of the State governments. For instance the State Government in Assam has been pro-active towards the needs of the ADC’s and hence has increased the powers and functions of the North Cachar Hills Autonomous Council and the Karbi Anglong Autonomous Council by transferring thirty (30) additional subjects to these District Councils through some amendments, whereas the State Government in erstwhile Assam under which three ADC’s were established and subsequently the State of Meghalaya have been keeping the ADC’s under tight control by restricting them to play a role only in respect to those provisions provided by the Sixth Schedule and not allowing them any greater area beyond the provisions of the Sixth Schedule. Rather, the state Government in Meghalaya has made good use of Paragraph 12(A) of the Sixth Schedule to keep the ADC’s under it check.

The Study Group has found that the assigning of functionaries and responsibilities to the ADC’s depends on the wisdom of the respective State governments. If the State Government finds it appropriate that the District Councils can better handle some affairs, then it may transfer some of the concerned subjects to the ADC’s, as has been done in the State of Assam. But it is seen that the State Government transfers powers and functions to the ADC’s only after much protest and agitations by the people living within the respective jurisdiction of the concerned ADC’s. One such example was the Karbi Anglong Accord dated 1-4-1995, between Government of India, Government of Assam, and the Tribal Bodies of Karbi Anglong and North Cachar Hills, whereby the Government had to transfer additional powers to the ADC’s. Another clear case are the immense powers given to the Boroland Territorial Council which came after a long struggle by the Bodo community.

A glance at the powers and functions of the ADC’s of different States would make it amply clear that there are variations within the ADC’s of the Sixth Schedule areas.

(a) The ADC’s of Assam

Below are the subjects assigned to the North Cachar Hills Autonomous Council and the Karbi Anglong Autonomous Council.
<table>
<thead>
<tr>
<th>No.</th>
<th>Department</th>
<th>No.</th>
<th>Department</th>
<th>No.</th>
<th>Department</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Industry</td>
<td>2</td>
<td>Animal husbandry and veterinary</td>
<td>3</td>
<td>Forest</td>
</tr>
<tr>
<td>5</td>
<td>Public Works Department</td>
<td>6</td>
<td>Sericulture</td>
<td>7</td>
<td>Education</td>
</tr>
<tr>
<td>9</td>
<td>Soil Conservation</td>
<td>10</td>
<td>Co-operation</td>
<td>11</td>
<td>Fisheries</td>
</tr>
<tr>
<td>13</td>
<td>Handloom and textiles</td>
<td>14</td>
<td>Health and Family Welfare</td>
<td>15</td>
<td>Public Health Engineering</td>
</tr>
<tr>
<td>17</td>
<td>Social Welfare</td>
<td>18</td>
<td>Flood Control</td>
<td>19</td>
<td>Sports and youth welfare</td>
</tr>
<tr>
<td>21</td>
<td>Food and Civil supplies</td>
<td>22</td>
<td>Town and Country Planning</td>
<td>23</td>
<td>College Education</td>
</tr>
<tr>
<td>25</td>
<td>Publicity and public relations</td>
<td>26</td>
<td>Printing and Stationery</td>
<td>27</td>
<td>Tourism</td>
</tr>
<tr>
<td>29</td>
<td>Excise</td>
<td>30</td>
<td>Finance including sales tax etc</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

The 30 Departments that have been transferred to the KAAC and NCHAC are as follows:

1. Industry
2. Animal husbandry and veterinary
3. Forest
4. Agriculture
5. Public Works Department
6. Sericulture
7. Education
8. Cultural Affairs
9. Soil Conservation
10. Co-operation
11. Fisheries
12. Panchayat and Rural Development including DRDA
13. Handloom and textiles
14. Health and Family Welfare
15. Public Health Engineering
16. Irrigation
17. Social Welfare
18. Flood Control
19. Sports and youth welfare
20. Weights and measures
21. Food and Civil supplies
22. Town and Country Planning
23. College Education
24. Land Reforms
25. Publicity and public relations
26. Printing and Stationery
27. Tourism
28. Transport
29. Excise
30. Finance including sales tax etc
(b) Below are the 40 departments that have been assigned to the BTC

<table>
<thead>
<tr>
<th></th>
<th>Department</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Industry</td>
</tr>
<tr>
<td>2</td>
<td>Co-operation</td>
</tr>
<tr>
<td>3</td>
<td>Forest</td>
</tr>
<tr>
<td>4</td>
<td>Agriculture</td>
</tr>
<tr>
<td>5</td>
<td>Fisheries</td>
</tr>
<tr>
<td>6</td>
<td>Sericulture</td>
</tr>
<tr>
<td>7</td>
<td>Education</td>
</tr>
<tr>
<td>8</td>
<td>Irrigation</td>
</tr>
<tr>
<td>9</td>
<td>Soil Conservation</td>
</tr>
<tr>
<td>10</td>
<td>Animal Husbandry &amp; Veterinary</td>
</tr>
<tr>
<td>11</td>
<td>Public Works Department.</td>
</tr>
<tr>
<td>12</td>
<td>Public Health Engineering</td>
</tr>
<tr>
<td>13</td>
<td>Handloom and Textiles</td>
</tr>
<tr>
<td>14</td>
<td>Health and Family welfare</td>
</tr>
<tr>
<td>15</td>
<td>Social Welfare</td>
</tr>
<tr>
<td>16</td>
<td>Cultural Affairs</td>
</tr>
<tr>
<td>17</td>
<td>Library Services</td>
</tr>
<tr>
<td>18</td>
<td>Tribal Research Institute</td>
</tr>
<tr>
<td>19</td>
<td>College Education</td>
</tr>
<tr>
<td>20</td>
<td>Weights and Measures</td>
</tr>
<tr>
<td>21</td>
<td>Lotteries, Theatres, Dramatic</td>
</tr>
<tr>
<td></td>
<td>performance and cinemas</td>
</tr>
<tr>
<td>22</td>
<td>Municipal corporation. Improvement</td>
</tr>
<tr>
<td></td>
<td>trust, district boards and other</td>
</tr>
<tr>
<td></td>
<td>local authorities.</td>
</tr>
<tr>
<td>23</td>
<td>Urban Development Town and</td>
</tr>
<tr>
<td></td>
<td>country planning</td>
</tr>
<tr>
<td>24</td>
<td>Panchayat and Rural Development.</td>
</tr>
<tr>
<td>25</td>
<td>Land Revenue</td>
</tr>
<tr>
<td>26</td>
<td>Publicity and Public Relations</td>
</tr>
<tr>
<td>27</td>
<td>Printing and Stationary</td>
</tr>
<tr>
<td>28</td>
<td>Markets and fairs</td>
</tr>
<tr>
<td>29</td>
<td>Food and Supplies</td>
</tr>
<tr>
<td>30</td>
<td>Town and country planning</td>
</tr>
<tr>
<td>31</td>
<td>Sports and youth welfare</td>
</tr>
<tr>
<td>32</td>
<td>Planning and development</td>
</tr>
<tr>
<td>33</td>
<td>Tourism</td>
</tr>
<tr>
<td>34</td>
<td>Flood Control</td>
</tr>
<tr>
<td>35</td>
<td>Statistics</td>
</tr>
<tr>
<td>36</td>
<td>Transport</td>
</tr>
<tr>
<td>37</td>
<td>Intoxicating liquors, opium</td>
</tr>
<tr>
<td></td>
<td>and derivatives etc.</td>
</tr>
<tr>
<td>38</td>
<td>Welfare of plain tribes and</td>
</tr>
<tr>
<td></td>
<td>backward classes</td>
</tr>
<tr>
<td>39</td>
<td>Relief and rehabilitation</td>
</tr>
<tr>
<td>40</td>
<td>Registration of births and deaths</td>
</tr>
<tr>
<td>41</td>
<td>Land Reforms</td>
</tr>
<tr>
<td>42</td>
<td>Museum and archaeology</td>
</tr>
<tr>
<td>43</td>
<td>Labour and employment</td>
</tr>
<tr>
<td>44</td>
<td>Food and Supplies.</td>
</tr>
</tbody>
</table>

(c) The powers of the ADC's in the State of Meghalaya

<table>
<thead>
<tr>
<th></th>
<th>Power</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Appointment/ succession of</td>
</tr>
<tr>
<td></td>
<td>Chiefs/Headmen</td>
</tr>
<tr>
<td>2</td>
<td>Construct/ manage primary schools</td>
</tr>
<tr>
<td></td>
<td>(withdrawn by the government)</td>
</tr>
<tr>
<td>3</td>
<td>Management of land &amp; forest.</td>
</tr>
<tr>
<td></td>
<td>(not R.F)</td>
</tr>
<tr>
<td>4</td>
<td>Control of money lending &amp; trading</td>
</tr>
<tr>
<td></td>
<td>by non-tribals</td>
</tr>
<tr>
<td>5</td>
<td>Marriage and Divorce</td>
</tr>
<tr>
<td>6</td>
<td>Inheritance of property</td>
</tr>
<tr>
<td>7</td>
<td>Ponds</td>
</tr>
<tr>
<td>8</td>
<td>Ferries</td>
</tr>
</tbody>
</table>
The powers and function of the Tripura Tribal Areas Autonomous District Council:

<table>
<thead>
<tr>
<th>No.</th>
<th>Function</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Finance, including local audit</td>
</tr>
<tr>
<td>2</td>
<td>Appointment and Services</td>
</tr>
<tr>
<td>3</td>
<td>General Administration</td>
</tr>
<tr>
<td>4</td>
<td>Law</td>
</tr>
<tr>
<td>5</td>
<td>Council Affairs</td>
</tr>
<tr>
<td>6</td>
<td>Local self government</td>
</tr>
<tr>
<td>7</td>
<td>Public Work</td>
</tr>
<tr>
<td>8</td>
<td>Rural development</td>
</tr>
<tr>
<td>9</td>
<td>Agriculture and allied services</td>
</tr>
<tr>
<td>10</td>
<td>Information, Cultural affairs, youth programmes, Sports science and technology.</td>
</tr>
<tr>
<td>11</td>
<td>Public Work, including rural water supply</td>
</tr>
<tr>
<td>12</td>
<td>Education, including Social Education</td>
</tr>
<tr>
<td>13</td>
<td>Industries</td>
</tr>
<tr>
<td>14</td>
<td>Fisheries</td>
</tr>
<tr>
<td>15</td>
<td>Tribal welfare</td>
</tr>
<tr>
<td>16</td>
<td>Co-operation</td>
</tr>
<tr>
<td>17</td>
<td>Health and Family welfare</td>
</tr>
<tr>
<td>18</td>
<td>Animal Husbandry</td>
</tr>
<tr>
<td>19</td>
<td>Forest, including horticulture</td>
</tr>
</tbody>
</table>

(d) Below are the functions of the ADC’s in the State of Mizoram:

<table>
<thead>
<tr>
<th>No.</th>
<th>Function</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Agriculture and horticulture</td>
</tr>
<tr>
<td>2</td>
<td>Fisheries</td>
</tr>
<tr>
<td>3</td>
<td>Public health engineering</td>
</tr>
<tr>
<td>4</td>
<td>Industry</td>
</tr>
<tr>
<td>5</td>
<td>Sericulture</td>
</tr>
<tr>
<td>6</td>
<td>Animal husbandry and veterinary</td>
</tr>
<tr>
<td>7</td>
<td>Arts and Culture</td>
</tr>
<tr>
<td>8</td>
<td>Social Welfare</td>
</tr>
<tr>
<td>9</td>
<td>Soil Conservation</td>
</tr>
<tr>
<td>10</td>
<td>Local administration</td>
</tr>
<tr>
<td>11</td>
<td>Forest</td>
</tr>
<tr>
<td>12</td>
<td>Transport</td>
</tr>
<tr>
<td>13</td>
<td>Sport and youth services</td>
</tr>
<tr>
<td>14</td>
<td>Co-operation department</td>
</tr>
<tr>
<td>15</td>
<td>Public Works department</td>
</tr>
<tr>
<td>16</td>
<td>Education</td>
</tr>
<tr>
<td>17</td>
<td>Rural development</td>
</tr>
<tr>
<td>18</td>
<td>Relief and Rehabilitation</td>
</tr>
<tr>
<td>19</td>
<td>DRDA and ICDS</td>
</tr>
<tr>
<td>20</td>
<td>Waterways and inland water transport</td>
</tr>
</tbody>
</table>
The above tables therefore give a clear picture of the Departments transferred to the ADC’s. There is therefore no common minimum consistency in the powers and functions of the ADC’s. The B.T.C which came into operation very recently, has been granted with some very important departments such as that of Labour and Employment, Welfare of the Plain Tribes and the Backward Classes and Tourism. These subjects are not to be found with other ADC’s. A glance at the powers and functions of the ADC’s of Meghalaya shows that they stand nowhere in comparison to the other ADC’s in spite of the fact that every ADC’s draw their strength from the Sixth Schedule. Thus as said earlier different ADC’s have different needs and that fact has been appreciated by some of the State governments.

One of the major problems being faced by almost all the ADC’s is that of financial constraints. The ADC’s have their sources of fund flow which are mentioned in the Sixth Schedule itself through Paragraph VIII and IX. A cursory view of these paragraphs will give us an understanding about the mobilization of resources through levy of taxes and share of royalties with the state government.

Paragraph VII talks about the powers to assess and collect land revenue and to impose taxes.

1. The Regional Council for an autonomous region in respect of all lands within such region and the District Council for an autonomous district in respect of all lands within the district except those which are in the areas under the authority of the Regional Councils, if any, within the district, shall have the power to access and collect revenue in respect of such lands in accordance with the principles for the time being followed by the Government of the State in assessing lands for the purpose of land revenue in the State generally.

2. The Regional Council for an autonomous region in respect of areas within such region and the District Council for an autonomous district in respect of all areas in the district except those which are under the authority of the Regional Councils, if any, within the district, shall have the power to levy and collect taxes on lands and buildings, and tolls on persons resident within such areas.

3. The District Council for an autonomous district shall have the power to levy and collect all or any of the following taxes within such districts, that is to say

(a) taxes on professions, trades, callings and employments;
(b) taxes on animals, vehicles and boats;
(c) taxes on the entry of goods into a market for sale therein, and tolls on passengers and goods carried in ferries; and
(d) taxes for maintenance of schools, dispensaries or roads.

(4) A Regional or District Council, as the case may be, may make regulations to provide for the levy and collection of any of the taxes specified in sub-paragraph (2) and (3) of this paragraph and every such regulation shall be submitted forthwith to the Governor and, until assented to by him, shall have no effect.

Paragraph IX talks about licenses or leases for the purpose of prospecting for, or extraction of, minerals.

(1) Such share of the royalties accruing each year from licenses or leases for the purpose of prospecting for, or the extraction of, minerals granted by the Government of the State in respect of any area within an autonomous district as may be agreed upon between the Government of the State and the district Council of such district shall be made over to the District Council.

(2) If any dispute arises as to the share of such royalties to be made over to a District Council, it shall be referred to the Governor for determination and the amount to be determined by the Governor in his discretion shall be deemed to be the amount payable under sub-paragraph (1) of this paragraph to the District Council and the decision of the Governor shall be final.

In spite of the above paragraphs mentioning about the process of mobilization of funds for the ADC’s, the fact remains that there is no parity with the devolution of funds and mode of fund flow for the ADC’s within the region. Different ADC’s have different requirements, so also the funds released to them by the Centre through the State Government varies accordingly. For instance the B.T.C has been given an additional grant of Rs. 100 crores per annum for five years besides other funds since its inception to accelerate development projects, but the same has never been the case with other ADC’s, and therefore, perhaps much to their concern.

The 11th and 12th Finance Commission had made provisions to give grant for the ADC’s, but through the respective State governments. The ADC’s have expressed their dissatisfaction to the Central Funds being routed through the State Government. This makes ADC’s totally dependent on the State Government for their finances. The ADC’s
point out that because of their dependence on the State Government for finances, they cannot execute the development activities, hence the demand for direct funding from the Central Government. The release of funds by the State Government is sometimes delayed to such an extent that it leads to the lapse of the small development projects undertaken by the ADC’s.

In the state of Meghalaya, the ADC’s have expressed their deep resentment over the treatment meted out to them by the State Government. The three ADC’s have pointed out that the share of royalties and taxes between them and the State Government and the ADC’s was 60:40 respectively. Recently this share has come further down to 75:25 for the State Government and the District Councils respectively. The Government does not give any detail of the royalty collected. The ADC’s argue that such undermining of their financial position by the State Government does not augur well for the overall functioning of the ADC’s.
F. Provision for two/three tiers of local governance and interface between ADC’s and Village Councils (including extant traditional institutions e.g. Dorbars and Syiem), between ADC’s and Deputy Commissioner, and between ADC’s and State governments.

The framers of the Constitution of India appreciated the diversity of the land and its cultural plurality. To ensure that the smaller tribes and communities’ life and culture were preserved, provision was made in the Sixth Schedule to ensure the place and respect of tribal cultures, in this case those of the North-East Region.

Traditional institutions of governance in North-East India as we have them today, originated among pre-literate communities in pre-colonial times. Consequently the tribes were not able to put in writing the powers and functions of the different forms of governing themselves. The numerous tribes and communities who inhabit the region have oral histories which have become useful in establishing their connection in the region since antiquity for some, to more recent times for others, and even to contemporary history for some migratory groups whose settlement in the hill and plains of this part of India has occurred in living memory. While it may be possible to reconstruct the pre-history of some of the tribes from study of their material remains, it becomes difficult to assign them ‘ancient’ and medieval’ pasts because there is an absence of written material from which to reconstruct their past. Even giving them a ‘modern’ history becomes difficult because to move into the modern without an intelligent account of what occurred before this period would be contributing to a fallacy in history. Mention has been made of these problems to put our understanding of traditional institutions in the North-East in perspective. For institutions to become tradition, a past that is somewhat long in time is required. This past varies for the tribes in the region. Khasi recall of their transient settlement in the Brahmaputra valley. Meiteis have assigned a fixed time of their recorded history to the fourth decade of the first century. It is not possible to assign a date to the Naga diaspora or to more recent movements of tribes such as the Mizo-Kukis whose settlement in the hill is of more recent origin. However historians can hazard tentative dates for these movements and settlements by judicious use of oral traditions cross-checked with other forms of information of a given phase of human history.

It is not certain when and why the institutions that the tribes came to accept as their own originated and under what circumstances. Much of what has been written on their origins is based on conjecture or on material that in all probability cannot be verified as being the
near to the truth. However, what is to be appreciated is that from their uncertain origins to the present, the institutions have stood the test of time. Today we are attempting to understand and revisit traditional institutions because as much as they appear outdated and obsolete they continue to function, not always in the desired form but nonetheless with societal support for both their usefulness and their social control. The earliest written references to the institutions were done by observers who saw in the numerous patterns of tribal government, forms quite different from their own and institutionalised systems of governance. Later, writers from among the tribes both elaborated and clarified the views on their institutions. There thing lay for some other than the occasional inquisitive academician still in search of answers to their own questions. Today the study of traditional institutions assumes significance as there is an attempt by the tribes to seek constitutional recognition of their institutions in a bid to fit the institutions into the modern system of government, of which more will be said later in this presentation.

The tribes developed the institutions of governance out of their own genius and perhaps after many trials and tests till they arrived at a form or forms of rule, which they considered good for themselves. Some changed the institutions started by them at later periods of their unrecorded past to adapt to changing situations while still others were applied by the British imperial rulers to suit the local situation in their new and imposed government.

The tribe that experienced the three stages of the development of the institutions was the Khasi-Jaintia. The basic unit of political organization in the Khasi-Jaintia society was the village, which composed of one or two decent groups. Village administration was conducted by an assembly of all resident adult males under an informal headman elected by them from among their number. When new villages were formed the new community did not detach themselves from the original village but remained an integral part of the growing state or Hima. Administrative and political necessity led to the institution of tribal leaders such as the Basan and Lyngdoh. The Basan was entrusted the conduct of the clan while the Lyngdoh was entrusted both administrative and sacerdotal functions. Under them they had Pators, Sangots and Matebors who assisted in the administration of the Shnong and the Raid. From this rudimentary beginnings it is believed, emerged the institution of Syiemship which probably arose out of voluntary association of villages when new developments such as the opening of markets, marriage laws, organization of land tenure and judicial administration brought in the need of a central and common ruler. The Basans and Lyngdohs who surrendered their powers as rulers did not forfeit all their powers as they and the founding clans of Himas, the Bakhraw, retained some of their administrative and religious functions, even retaining in some Himas the privilege to elect their Syiens.
In the origins of Syiemship there was adaptation as some early Syiemhs were drawn from the people of non-Khasi origin. One Khasi Hima has Wahadadars, an institution the people of that state have borrowed from nearby Bengal prior to British rule. And when the British extended their political control over these hills they instituted another functionary, Sirdars over certain other Himas. Adaptation is also evident in the Naga functionary, the Gaonbura and the Arunachal Dobashi and the Garo Laskar. This should suggest that the institutions evolved over a long period of time and were perforce to adapt and change in some of their functionaries by circumstances over which they had little control.

The higher rung of the hierarchical structure [it reminds us that the tribal societies were not egalitarian as it was believed to have been by many writers] of the tribal communities was dominated by their chiefs and assisted by tribal councils. We have made reference to the Khasi-Jaintia structure. The Garos evolved the institution of the Nokma—there are four kinds of Nokmas, the Gamni Nokma; the Gana Nokma; the Kamal Nokma and the A’king Nokma—only the last of the four was entrusted with governing the village. The Garo institutions just as the Syiem of the Khasi Hima of Khyrim are somewhat unique. Whereas the other institutions are patriarchal in nature, the Nokma is subject to Garo laws of inheritance through the female line, the Mahari; while the Syiem of the Khasi hima referred to is directly related to the Syiemad of that state. It is not possible here to go into all the institutions prevailing in tribal North-East India. It may suffice to take some case studies to explain the nature and function of the living patterns of tribal people governing themselves.

The Naga institutions of chief as it exists today have come down through Naga life over years and under conditions which would have only allowed for strong men as their chiefs. A recent report has summed up the Naga position thus: “The traditional system of Naga polity … varies from autocracy (Konyaks), gerontocracy,(Aos, Tangkhuls) and democracy (Angami, Chakhesangs, Rengmas, Maos). Among the Semas, the position of the chief is a little less arbitrary than the Konyaks, but is nevertheless highly autocratic.” This rather simplistic explanation of the prevalent situation in the Naga hills inclusive of the Naga inhabited areas within Manipur state overlooks the fact that succession to the position of village chief is usually hereditary except among some tribes. The moot point is in their functioning—while many of the chiefs take support from the adult male population of the village, in discussion and consultation through the village councils - the authoritarian Konyak Angh and the Sema Akeko are not bound to follow in like manner.
Whatever may be their structure at the top, the tribal societies put safeguards in their
governments through the village councils which performs the work of administering the
village, cluster of villages or the larger conglomeration. With their different names they
nonetheless have similar functions, administration of justice according to customary laws
and practices; keeping watch and ward, arranging the cycle of the jhum fields where this
practice is prevalent; overseeing the use and distribution of water and other resources; to
name some of the functions. Khasi Syiems were entrusted magisterial duties within their
own Himas by the British India government. This judicial function continues to be given
by the Indian administration though with reduced disposal of civil cases.

What we refer to as traditional institutions must have been a matter of everyday life for
the societies under review. They lived with their own structures under conditions of
privilege for certain section of the society or of oppression and exploitation to the larger
numbers. The institutions built up were particularly not fair to their women. They could
not aspire for positions of leadership, they were denied entry into the councils and were
not heard or consulted. They could not participate as equals to their men-folk in these
tribal societies. The literature that is now available on the position of women in the
traditional tribal societies suggests that tribal women were not as exploited as their
counterparts in mainland India - but it does not speak well of the tribesmen to have given
secondary position to their women.

The institutions briefly reviewed above are now faced with a dilemma - to change in part
or substantially and to further adjust into the changed circumstances within which they
have survived. Faced with these problems these institutions are threatening to adjust and
change with the times or become set, rigid and moribund. It is as if they are now
unchangeable. And all this despite the fact that the chiefs, village and council elders and
the different functionaries of the tribal societies have been opened to the many changes
and influences that would make them enlightened - to use the expression.

In part the hardening of the traditional leaders to the changes they face comes as a reaction
to the unsympathetic if not unconcern the Indian State gave them over the past five
decades. The Indian State lost sight of the role traditional institutions could have played
in the administration of the tribal people in a more effective manner. It did not take the
lessons from the British who had used the chiefs and their councils as useful instruments
in what has been called ‘indirect administration.’ Rather than utilise the experience of
their leadership, a new institution in the District Councils was introduced under the Sixth
Schedule of the Indian Constitution, composed of elected representatives of the tribal population to oversee as part of their functions, the working of the age-old traditional forms of government. With the introduction of the District Councils the situation has actually deteriorated to mistrust of one institution for the other; a misuse of power by the newer form of administration which has in most cases failed miserably. It is no surprise therefore that we are witnessing in our own time a resurgence of the rights and powers and privileges of the traditional institutions and their leaders.

The traditional leaders of the tribes of the region were once powerful and respected. Much of that power and respect went with the promulgation of the Constitution of India. Interestingly the traditional leaders continued their role in administration of their respective tribes without any formal role. Society saw a need for their role. The traditional leaders, for want of a better term, were accommodated in the administration without constitutional recognition and without serious disadvantage to themselves and the State. Of late thought the State governments have been using the traditional leaders as useful instruments at the village and conglomerate level of administration. The leaders therefore want both recognition and Central funding.

Recognition should be formalized and constitutional recognition applied after considerable thought. While it must be appreciated that the traditional leaders’ role has increased in the administration of their own tribes, no tribe today lives in such exclusion as of old. The question may therefore be asked what role may these leaders play in a society that has become plural and complex? Within the tribal societies there are sections that see no purpose and requirement of the traditional leaders. The Mizos did away with their Lals in what was a popular movement in the early 1950s.

In 2000, there began a development in the Khasi Hills and particularly in Shillong to revive the position of the Syiems. The Federation of Khasi States (Himas) was revived under a different nomenclature. Efforts were made to involve the Nokmas of the Garos and the Dollois of the Jaintia Hills. The Garo Nokmas have set up a Nokma Council in Tura. This Council has its own building where representative Nokmas meet. What effect the trends in the Khasi, Jaintia and Garo hills have had on the traditional leaders of the other hill and plains tribes of the region is not ascertained.
One demand of the Federation of Khasi States continues to be that of Central funding for the Khasi Himas. There is a lukewarm move from the leaders of the other two hill areas of Meghalaya on this issue. The Khasi states do not have the infrastructure to place development as an agenda. They do not, other than the larger states have the administrative experience of accounting. They have not been receiving government funds for development as there already is in place mechanisms to manage development of village and their conglomerates. Some questions may be asked. How will these traditional instructions and their durbars be made accountable if direct finding is given to them? Why should representatives of the people who are not elected by the adult population of the states take control of funds and their expenditure? Can traditional institutions not adjust in time to the fast pace of changes?

2: The appropriateness of the Nagaland model of communalizations based on Village Councils and Village Development Boards

Nagaland which is neither under the Sixth Schedule or Parts IX and IX A of the Constitution has its own traditional system of village bodies. Nagaland was established on 1st December, 1963 following an agreement reached by the Government of India with the leaders of the Nagaland People’s Convention in July 1960, under which it was decided that the Naga Hills – Tuensang Area, a Part ‘B’ Tribal Area within the State of Assam would be formed into a separate state. The state of Nagaland has a special status through the 13th Constitutional Amendment in 1962 wherein Article 371-A was inserted to provide that no Act of Parliament in respect of religious or social practices of the Nagas, Naga Customary Law and Procedure, Administration of Civil and Criminal justice involving decision according to Naga Customary Law and ownership and transfer of land and its resources would apply to the State without approval from the Legislative Assembly of Nagaland.

With a strong sense of community inborn in all Nagas, there have always been traditional village institutions for self – governance in Nagaland. Nagaland which does not fall under the purview of the Sixth Schedule, Fifth Schedule or Part IX, IX A has its own unique model of ‘communalization’ based on the Village Council and Village Development Boards (VDB’s). Nagaland has been uniquely placed in the scheduled states as the Naga leaders rejected the proposed Sixth Schedule scheme that is functioning in many states of North East including newly created Territorial Councils. Instead Nagaland was given special concession and the Village Councils, Area councils were formed for local self governance.
Nagaland involved a single tier local body system, confirmed to Village Councils alone through The Nagaland Village Council Act 1990. Under this Act, every recognized village, established according to the usage and customary practices of the population of the area is required to have village councils (V.C), with a five year term. The council consists of members, chosen by villagers in accordance with the prevailing customary practices and usages as approved by the State Government. The Act provides that hereditary village chiefs shall be ex–office members of such Councils. It is the job of the village council to formulate village development schemes and other welfare activities to help Government agencies in carrying out development works in the village and to take up development works on its own initiative or on request by the Government.

The Village Council also has the power to administer justice within the village limits in accordance with the customary law and usages and has full powers to deal with internal administration of the village.

The operation of Village Development Board (VDB) is a very unique experience in the State of Nagaland. In essence, it means giving power to the people to plan development schemes for themselves, which is commonly called grass-root planning. This is in clear contrast with central planning that the country after Independence has been following. After several decades it was found that centralised planning was not really in touch with the grass-root level of society and their reality. In fact, many plans have been responsible only in widening the gap between the rich and the poor. Therefore, an experiment was made in many parts of India including Nagaland to have Village Development Boards.

**Origin of VDB:** The spirit of socialism had a strong base in the state of Maharashtra and Gujarat in the early days of the post-Independent India. It was, therefore, the idea of those idealistic socialist leaders who propagated the need to share the wealth of the State equally between the rich and the poor. In order to achieve this, some fundamental grass-root planning which resembled the existing VDB type of schemes were tried out in other parts of the country. The experiment could not succeed because the recipient villagers were too thinly spread out and not cohesive and compact, as it is in Nagaland.

It is for these reasons that this brilliant idea failed to strike root both in Maharashtra and Gujarat. However, a significant turn was felt in Nagaland when Shri A.M. Gokhale, I.A.S, was posted to Phek District as its Deputy Commissioner. Being the son of the famous socialist Leader S.M. Gokhale, he began to toy with the idea of introducing the failed experiment of Maharashtra and Gujarat in Phek District of Nagaland. He was positive
that the idea of a village developing its own needs and requirements will surely prove to be effective. He was also encouraged by the close social setting of the people within a compact ecological spread. He also studied as to why the generous funds that were been doled out to the state were not percolating down to the villages in particular. In this context, Shri A.M. Gokhale realised the crux of the problem and tried to devise a system in such a way that various funds being allotted will go directly to the people to be planned and utilized according to the local needs. This also disallows the funds meant for the villagers to be exercised by high government officials at their own discretion. This was how V.D.B. took its root in Nagaland.

He also formulated a model draft and a model rule which was circulated to a select group of officers to draw useful critical appraisal on the basis of which he could finally distil the idea and after securing the approval of the State cabinet, the V.D.B. took its foundation. Phek District was the first test pilot area for VDB in action. It started at Ketsapomi Village in October, 1976. After a little over one year of implementing the VDB schemes throughout Phek District, it showed phenomenal positive results. VDB scheme became an instant success which prompted the State Government to adopt the VDB throughout the State of Nagaland. In gradual progression, according to positive results shown, VDB allocation of fund per house-hold was raised from Rs.100/- to Rs. 200/- to Rs. 750/- to Rs. 800/-, out of which 25% is earmarked for women activities and 20% is earmarked for youth activities. There are 1086 number of VDB's existing in Nagaland.

The topic of VDB, of late, is not a very open subject as there have been cases of misappropriation, infiltration of party politics and bureaucratic influence within the VDB and its functionaries. Despite these drawbacks, the VDB concept is still recognised to be the main democratic process of grass-root planning in the State of Nagaland.

There are two main sources of funds for the VDB's. (i). Matching grant schemes: the Government's contribution to the villagers common fund is equal to the amount of the common fund raised by the villages which are invested for a minimum of 5 years in fixed deposit accounts in the banks followed by continuous re-investments. (ii)Grant-in-aid: The department of rural development in Nagaland allots part of the state Government's annual plan fund village wise instead of sector wise allotment as is the common practice in other state of India. This ensure recurring source of funds to the villages. (iii)The VDB's source of income is also through centrally sponsored funds for Integrated Rural Development
Programme (IRDP), State Rural Development Agency (SRDA) also implements IRDP and allied programmes. The VDB’s are recognised as its field agencies and subsidy amount is directly released for the same. Consequently rural development department also includes schemes for women.

A young scholar who is studying the development process in Nagaland has appreciated the Village development Boards which are perhaps the only decentralized institutions that have given representation to women. In the traditional set up, women were not permitted to become village goanburas. The Village Development Boards provide for one fourth of their members being women. However this has remained a legislative incorporation as not all village have made provision to have women in their boards. Even if women are represented they do not take part in financial and decision making matters.

The VDB’s were constituted with two main grants, matching grants and grants in aid. To this has been added the decision to disburse grants under the NREGS, JRY etc. The VDB in association with the Village council are made responsible for identifying potential beneficiaries. This has given the members of the VBBs and the Village Councils tremendous powers in the Naga villages.

To be fair to the VDB’s they are not in conflict with the traditional authority structure in Naga society as they have only financial and development functions- they have been provided financial decentralization, unlike the ADC’s that have legislative, judicial and administrative powers. However their functioning over the past three decades has posed innumerable challenges. The VDB’s are not distanced from the power structure within the villages. Rather they form an integral part of village politics. Moreover the decentralisation of financial powers has not necessarily led to grass root empowerment of the community. Patronage, privilege and power in the operation of the VDB’s have added a new dimension to the functioning of the village not necessarily in the desired manner.

The Village Development Boards were introduced in Nagaland in the absence of other controlling structures such as the ADC’s. The leaders of the erstwhile Naga Hills District of undivided Assam did not accept the Sixth Schedule. For want of any other pattern of village administration, the VDB’s have been tested and made applicable to the Naga context. It has had fair amount of success. This pattern of local governance also has its critics. How far this pattern of administration will be applicable to the hills and plains under the ADC’s is a question that is difficult to answer. The areas under the 10 ADC’s already have in place their own pattern of administration by their traditional leaders.
Superimposing the Nagaland model of VDB’s and replacing the existing pattern of local administration may not be prudent.

Demands for Autonomous District Councils

An interesting feature of the ADC’s in the region is that there is a move from three distinct tribal inhabited areas of Arunachal Pradesh to have ADC’s. This, despite the operation of Panchayati Raj in the State of Arunachal Pradesh.

The Proposed Patkai Autonomous District Council (Tirap and Changlang)

The region inhabited by the tribes with population of 225748 (2001 census) has tremendous scope for development of power, tourism, horticulture, mineral, mining etc. This area has remained isolated and has not received any focused attention particularly in the fields of education and infrastructure development. The negligible representation in various State governments and other organization from these major tribes is one of the sad testimonies of the above facts. Thus, the two districts remained backward and underdeveloped in every spheres of development and still continue to be so.

In order to ensure economic, educational and linguistic aspiration of the major tribes of the two districts and also to ensure preservation of their rich and unique socio-cultural, religious and ethnic identity, their leaders have made representations for separate District Councils for the tribes. There is a popular demand for a Patkai Autonomous District Council (P.A.D.C.).

The idea of autonomy as conceived in the case of Tirap and Changlang is the model that has been put into operation for the tribes of Tripura, the Boros and the Karbis. The demand for ADC’s is necessitated by the special situation of the place and people, politically, economically and in other aspects. The geographical position of these tribal areas and their location on the international border has called for some special attention.

The objectives of having an autonomous self governing body to be known as Patkai Autonomous District Council within the State of Arunachal Pradesh are: to fulfill the economic, educational and linguistic aspirations and the preservation of socio-cultural and ethnic identity of the indigenous tribes of the two districts of Tirap and Changlang and to speed up the infrastructure development in the districts.

The smaller tribes beginning with the Idus in Dibang Valley, those in Lohit, Changlang and Tirap who follow different traditions are very poorly represented in the administration.
and whose voice is very little heard on the Arunachal scene. Apparently, what the demand centres on is that the two district should have more numbers in the Arunachal administration. Here too like in some other existing ADC’s, the Councils are looked upon as employment agencies with little thought on the mandate and purpose of the ADC’s.

Likewise there is a demand for a proposed Mon Autonomous District Council (M.A.C.). West Kameng District as a whole is dominated by mountains/hills except little plain area in the foot hills adjoining Assam. In such land locked rugged topography the only source of accessibility is through existing poor network of road transport which hardly reaches to Circle/Block IIQ only. This means most of the villagers are still without assured, connectivity and villagers are in pockets of isolation which needs more attention and care for their all round development. The economic development depends upon how resources are mobilized. For this, there is need of timely planning and quick delivery mechanism so that sustainable development takes place at the local level.

This district is inhabited by numerous heterogeneous tribes which is different from each other in every aspect of their social life. There are Monpas, Akas, Mijis, Sherdukpens and Buguns. Numerically all of these tribes are in small numbers in comparison to other tribes of Arunachal Pradesh. But from time immemorial they have their own culture, religion and rituals, faiths and believes and handicrafts which are unique to each tribe by itself and to keep alive these values special protection and promotion are felt indispensable.

By virtue of being smaller in terms of numbers of population, all the tribes of this district have very less number of representatives and senior level officers at the apex body of decision and policy making. Similarly resource allocation is also not adequate or at par with the “degree of backwardness”.

West Kameng District has a very strategic location. It lies on the international boundary with China and Bhutan, having links through vital passes and valleys. The Chinese aggression into this region if fresh in the minds of the people who were affected by this intrusion. Therefore, this district draws special attention of planners and policy makers towards its people not only for materialistic development but also for promotion of emotional oneness with the mainland.

Modern education reached to this part of State late-as late as the 1960s. Consequently there are not many educated people in this remote part of Arunachal Pradesh. Human resource development is vital aspect and occupies Central place in the whole process of
development. But due to lack of awareness and motivation, people in the remote villages still prefer to engage their children in some of their domestic works for immediate benefits instead of sending them to the schools. So, unless special drive to raise the level of thinking and motivation is ventured the education scenario of the district will not improve and therefore the level of participation of the grass root level people in the development process will not be forthcoming.

Thus, taking into consideration of above facts and circumstances, if autonomous planning at the local level is granted it will in all possibility go a long way for the furtherance of interest of the tribes inhabiting this region in preserving their rich traditional cultural heritage, old aged religions, indigenous faiths and believes, valuable arts and handicrafts with which the people of this district will be able to preserve its own identity. Over and above, this will also help in removing regional disparities and provide insights to the people of this district in particular and Arunachal Pradesh in general of harmonious and equitable concept of living.

In the event of Panchayat Raj system ceasing to be in force in the area covered by the two districts, the powers of the Panchayat Raj institutions in the P.A.D.C. area shall be vested with the Council.
Conclusion

The core philosophy of the Sixth schedule of the Constitution was aimed at the protection of the tribal areas and their interests. Hence the ADC’s and the ARC’s were set up for various hill and plain areas of the North Eastern Region in 1952. These institutions are entrusted with the twin tasks of protecting tribal culture and customs and also undertake some development activities for the tribal areas. With so many years past since the operation of these Councils it has become necessary to review the functioning of the Councils and to vision their continued role without any changes in their structure with considered changes. The role of the ADC’s continue but with a new perspective to keep pace with the changing times. It was expected that the ADC’s would not only play an important role in protecting, preserving and promoting their respective cultures, but also play a vital role in the process of grass root development.

The institution of the Autonomous District Councils was set up by the Government of India under the provisions of the Constitution of India for very specific purposes. In the sixty years and more of the operation of the Constitution of India several amendments were made to the Sixth Schedule. In view of the different powers and functions of the several ADC’s in the North East it may be necessary for further amendments to be made taking into consideration a series of reports and perspectives of the ADC’s.

From the Study above some salient points emerge which may be considered by the Commission for Centre-State Relations.

1. As these Councils receive grants from Government, amendment may be introduced in the Sixth Schedule to provide for representation of women in the functioning of these Councils. This may come in the form of reserving a specific number of seats for women in each Council.

2. Ordinarily, it may be assumed, the membership to the ADC’s was meant to be filled by tribals of a particular community. The run up to the ADC elections in Meghalaya earlier in the year had reports of a large number on non-tribals of the Garo Hills putting in their papers as candidates for the different seats of the Garo Hills autonomous District Council. It is reported that of these many, one person not of any tribal community of the Garo hills has been elected from Phulbari Constituency as Member of the GHADC. While this apparently is in order, this is a first instance of a non-tribal, other than nominated members representing a constituency. This
raises issues which may have long standing impact whether there should now be reservation of seats to the different ADC’s only for the tribal communities.

3. It was perhaps not intended that the ADC’s were to be political bodies. The infusion of modern politics has in many cases not been conducive to the functioning of the ADC’s. Some serious thought may have to be applied to reduce, if not remove the political maneuverings within the ADC’s to ensure better functioning of these bodies.

4. The powers and functions of the ADC’s should be reviewed since more than 57 years have passed between the operation of the first of the ADC’s and those brought into operation more recently. The Study has made special note of the status of the ADC’s of Meghalaya whose powers and functions have not been enhanced since their establishment. The complexity of the situation is that these three ADC’s are entrusted the care of the traditional institutions, which are presently reasserting their positions. There may be a relook at some of the functions transferred to the ADC’s such as those relating to ferries, tolls, ponds, education etc.

5. NEHU organized in 2004 three Capacity Building Programmes for members of the Khasi, Jaintia and Garo Hills ADC’s. That experience gave tremendous boost to the Members of the ADC’s in understanding their position and powers. Several other members complained that they were not given an opportunity to attend! At the closing function of the programme in NEHU in December that year it was suggested that Capacity Building programmes be held for each of the three ADC’s once every term and that to go beyond this, similar programmes be held for the traditional leaders including the Syiemns, Dollois and Nokmas. In similar fashion, Capacity Building programmes may be organized in each of the ADC’s, once every term to enable newly elected members to attend and that similar programmes also be organized for the traditional leaders in each State of the region. This may be organized by select Universities in the region. The IIM, Shillong too may be requested to organize a programme once every other year for the Member and Officials of the ADC’S, particularly relating to human resources and financial management and other related matters.

6. The Study above clearly shows a lacunae in the planning for the ADC’S. Each of the ADC’S should be required, if not already done, to have Planning Boards which may function in synergy with the respective State governments.

7. A suggestion was given by one of the ADC’S that there should be a nodal agency to coordinate the functioning of the several ADC’s. The North Eastern Council is the regional planning body for the North-East. It may be prudent to
have a cell in the NEC to monitor the grants and the functioning of the ADC’s and to coordinate between the ADC’s and the respective State and Central governments.

8. Diversion of funds for purposes other than what they are sanctioned for is a serious issue. Recently it has come to the notice of the public through newspapers that the North Cachar Hills ADC was reported to have diverted a huge sum of money to militants operating in North Cachar Hills District. There may be other cases of diversion and not to the scale reported above. The case reported indicates the lack of transparency of the funds received and utilized. ADC’s should be required to annually submit annual reports including financial accounts and utilization certificate to their respective Governments with a copy to the Government of India/ NEC should the suggestion placed above be implemented. The Annual Report of the ADC’s will enable authorities to monitor the functioning of the ADC’s.

9. The Study team has noted the large numbers of persons employed in the several ADC’S. The output of the hundreds of staff and officers is not commensurate with the output of the ADC’S. While not suggesting the numbers be reduced, the ADC’S may be informed to restrict the number of staff and officers and other functionaries so that the ADC’S do not appear to be employment agencies.

10. Several studies have been made on the ADC’s by different agencies of the State and Central governments. Amendments of the Sixth Schedule have been made occasionally to update the powers and functions of the ADC’s. The salient aspects of each of these reports may be put together to arrive at a decision on the strengthening of the ADC’s.

11. It may be noted that while tribals have had the benefits of the ADC’S, there are numerous other of the same community who do not enjoy the provision of protection enshrined in the Constitution under the Sixth Schedule largely because they reside beyond the boundaries of an ADC. Such is the situation in Assam where many tribals such as the Bodos are scattered across the State. Large numbers of Garos live in Assam and therefore do not have the benefits of the provisions of the Sixth Schedule. Khasis and Jaintia live in Kamrup and Karbi Anglong districts and the districts of south Assam. They too do not enjoy the status others of the tribe enjoy in the hills. Similar is the situation in Tripura. And there are many more cases. How will these tribals be protected is a moot point and requires deliberation and policy decision.

12. The section on the appropriateness of the Nagaland model of communalizations based on Village Councils and Village Development Boards indicates that the model
may be introduced in the other hill areas of the region with some thought considering the present operation of the model. Likewise there are numerous demands for setting up ADC’s for other tribes in the region. While it would be fair to say that what one or several tribes enjoy through their ADC’s should be given to other kindred peoples. However their demands/request may be examined in the background of the functioning of the existing ADC’s.

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With inputs from Resource Persons at Shillong, Guwahati, Itanagar, Silchar, Diphu, Kohima, Agartala, Lawngtlai, Kamalnagar and Saiba
North Eastern Hill University  
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Shri V. K. Duggal  
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Commission on Inter-State Relations  
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27 June 2009  

Sir,  

The Commission on Inter-State Relations, Ministry of Home Affairs, Government of India, had requested the North-Eastern Hill University to undertake a **Study on Functioning, Structure of Local Governance in North Eastern Region with Special Reference to Autonomous District Councils/Autonomous Regional Councils**. The Study was undertaken from early this year after the sanctioned advance of Rs 2,48,000 (vide letter No. 1-35/2008/CCSR dated 19 January 2009) was received. A team of scholars and researchers have contributed to the study which is submitted herewith. The final utilisation of accounts will be submitted after approval of the final Report.

The Study Team puts on record its appreciation to the Commission on Inter-State Relations for selecting NEHU to undertake the Study.

Thanking you,  

Yours faithfully,  

Prof. David R. Syiemlieh  
Prof. L. S. Gassah  
Dr. A.K. Thakur  
Mr. D. Borkotoky
Taxation of Goods and Services in India
Acknowledgements

The Commission on Centre State Relations has been asked to examine as part of its Terms of Reference (ToR): ‘the need and relevance of separate taxes on the production and on the sales of goods and services subsequent to the introduction of value added tax regime’. This study deals with this Term of Reference. We are thankful to the Commission of Centre State Relations for entrusting this study to the Madras School of Economics. We have benefited considerably from interactions with the Hon’ble Members of the Commission on Centre State Relations and other officials during the course of this study. We would like to place on record our thanks to Shri Dhirendra Singh and Shri Vijay Shankar, Hon’ble members of the Commission with whom we had occasion to discuss the subject extensively.

We have considerably benefitted from discussions with late Dr. R.J. Chelliah and Dr. Amaresh Bagchi. We are also thankful to the participants in a seminar at the Madras School of Economics on Issues before the Finance Commission held in 2009, particularly Dr. Satya Poddar.

In the preparation of the manuscript we have been helped considerably by Ms Sudha and Ms Jothi at the Madras School of Economics.

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Taxation of Goods and Services in India: Present Arrangements

1.1 Introduction

The Commission on Centre-State Relations has been asked as part of its Terms of Reference (ToR) to examine ‘the need and relevance of separate taxes on the production and on the sales of goods and services subsequent to the introduction of value added tax regime’. In a federal economy like India, there are three issues that require examination in the context of this term of reference:

1. Whether there is any need or relevance for separation of production from sales in the case of goods.
2. Whether there is need or relevance for separation of goods from services in the context of taxation in a value added tax system.
3. Whether there is need or relevance for separation of jurisdictions of the Central and the State governments in capturing the value added in the production and sale of goods as well as services.

In this Chapter, we look at the existing system of taxation of goods and services in India, and the reforms that have led to the introduction of the Value Added Tax (VAT). In Chapter 2, we examine the continuing problems and the need for further reforms to bring about a comprehensive Goods and Services Tax (GST). In Chapter 3, we examine some of the available options in regard to the form of GST that can be adopted in India. In Chapter 4, we provide the concluding observations.

1.2 Goods and Services: Value Added in the Production and Sale

The economic activities, in a modern economy, lead to the production and sale of goods as well as services. Production of a good or service requires a number of inputs, which are themselves goods and services. If the value of inputs is more than the value of the produced good or service, there is ‘value added’ in the process of production. Once a good or service is produced, it travels to the final user through a sales chain consisting of wholesalers and retailers. At each stage, there would be some additional value added. The value of the final product would be the sum of the value added at the different stages in the production-sales chain. The distinction between goods and services can often be
blurred. Access to goods can be even in the form of a service. Services may be needed as inputs for goods and goods may need services as inputs.

The idea in VAT is to tax the value added at each stage up to the sale to the final consumer so that eventually the total value of the product is taxed. In this sense, it amounts to a retail sales tax. However, the difference is that in following the principle of taxing at every stage and rebating at every stage, it creates a paper chain of transactions and thereby minimizes the risk that any sales may be done outside the tax net.

### a. Understanding VAT: An Example

The VAT may be understood by tracking the stages of production and sale of a good or service. Various inputs are required in the production of a good or service. Together, these inputs, utilized in a production process produce an output, which is different and distinguishable from all the inputs that were used in its production. After the good/service is produced it will travel to the consumer through a chain of wholesalers and retailers or it will be used as an input into the production of other goods and services.

In a VAT system every time a sale of the good/service takes place, the value added tax is levied. But it is levied only at the value added and not at the gross value. As long as the good/service remains within the production process, it will be taxed in a manner such that the tax paid on it at any previous sale is rebated and tax falls only on the value added. Finally, the tax will be only on the sum of the value added in each step in the production/sales chain and will not at any stage be a tax on a tax previously paid. An arithmetic example is explained in Table 1.1.

Supplier A produces wheat flour from wheat which is valued at Rs. 100. This he sells to Supplier B at Rs. 110, which includes the 10 per cent VAT on value addition. The supplier B in turn adds value to the extent of Rs. 50 for transforming the flour into bread, here again the value added is taxed at 10 per cent which amount to Rs. 5. The supplier gives it to the marketing outlet who adds a profit to Rs. 22. At this stage the cost of bread is Rs. 172. The market outlet pays a tax of 10 per cent which amounts to Rs. 2.2. The total VAT paid on bread by the consumer at 10 per cent is Rs.17.2 which goes to the Government.

### b. Tax Base of Goods and Services in India: Three Segmentations

Considering the value added of goods and services taken together in the overall Indian economy as providing a comprehensive tax base, there are three kinds of segmentations
that take place in India under the existing arrangements: segmentation of goods from services, segmentation of Central jurisdiction vis-à-vis State jurisdictions, and segmentation of production/manufacture from sale. These artificial divisions for purposes of taxation lead to various distortions, administrative and compliance costs, and inefficiencies. These are also not consistent with prevailing tax practices in the modern economies of the world who have implemented a VAT regime including federal countries. A federal fiscal arrangement however places additional challenges because there is a need to examine the necessity and rationale of further reforms in the context of maintaining the fiscal and revenue autonomies of the two tiers of government.

Table 1.1
Value Added Tax on Bread

<table>
<thead>
<tr>
<th></th>
<th>Cost</th>
<th>Tax Paid by Supplier/Consumer</th>
<th>Value Added</th>
<th>Tax Received by Government</th>
<th>Tax Rebated by Government</th>
</tr>
</thead>
<tbody>
<tr>
<td>Supplier A produces flour</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cost of flour</td>
<td>100</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Supplier A sells flour to producer B charges VAT on flour at 10 %</td>
<td>10</td>
<td>10</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>B pays to A</td>
<td>110</td>
<td>10</td>
<td>10</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cost of other inputs</td>
<td>50</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>VAT on other inputs at 10 %</td>
<td>5</td>
<td>5</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>B pays for other inputs</td>
<td>55</td>
<td>5</td>
<td>5</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Profit margin on cost exc. VAT at 20 %</td>
<td>22</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Value added</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cost of bread</td>
<td>172</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Value added</td>
<td></td>
<td>22 (=172-150)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>VAT on value added</td>
<td>2.2</td>
<td>2.2</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>VAT paid on Bread by consumer at 10%</td>
<td>17.2</td>
<td>17.2</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
The Central government levies Cenvat, which covers value added in the case of production and sale of goods up to the stage of ‘manufacturing’. State governments, on the other hand, are entitled to capture the value at the stage of sale. This value covers the value added at different stages in production/sale cycle covering stages of manufacturing, wholesale, and retail stages that may be more than one. The taxation space up to the value added in the production of goods is common between the Centre and the States. Different states can have their own variations in terms of rates and classification of goods. In the State-VAT system, an attempt has been made to arrive at a broad convergence of rates, but states have gone for their own classification schemes and there are many differences in the classification schemes. In addition to the State-VAT, the levy of a central sales tax continues on inter-State sales.

While the system of taxation is thus characterized by fragmentation and overlaps in the case of goods, the taxation of services remains separated and disjointed from that of goods. The service tax is levied by the Central government. With different tiers of government involved in taxation of value added in the case of goods, there is considerable cascading that result. Cascading means taxation of tax already paid. Cascading is a feature of a tax system that causes several inefficiencies and distortions. In particular, it favours imports, which are treated as final goods and bear the burden of taxation only once, against domestic production, which may be taxed several times; it increases the cash balance requirement of the producers/dealers; it makes tracing the overall tax burden of a good or a service difficult; and, it encourages tax evasion and compliance costs.

Taxation of goods by either tier of government may cascade into taxation of services and vice versa since goods may be needed in the production and sale of services and services may be needed in the production and sale of goods. The nature of a modern economy is such that it is often difficult to draw lines between goods and services as these are embedded into each other.

In this overall context, this study examines the system of taxation of goods and services in India. It provides an overview of the evolution of the domestic system of taxation of goods and services and the reforms that have taken place since the nineties. It then describes the system that has emerged after this first generation of reforms and its shortcomings as judged from theoretical norms as well as international practices. The study then goes on to argue for further reforms. It argues that there is no need or rationale to continue to maintain the distinction between goods and services and there is
a need to further reform the system to bring about a comprehensive and integrated system of taxation of goods and services, which may augment the income and welfare of the society.

1.3 First Principles of a Good Tax System

In the well-known Public Finance Text, Musgrave and Musgrave (1973) describe the following as characteristics of a good tax system:

1. **Adequacy of Revenue**: The tax system should be revenue productive in a manner that the Government is able to finance the provision of public and merit goods to the desired extent.

2. **Equitable Distribution**: The tax system should be such that everybody pays his fair share of taxes according to their ability to pay. This issue should be considered in terms of final incidence of tax.

3. **Minimum Distortions**: Taxes should be chosen so as to minimize interference with economic decisions relating to allocation of resources in markets that may otherwise be efficient. In fact, taxes impose excess burdens, and the design of the tax system should be such that these are minimized.

4. **Facilitation of Stabilization and Growth Objectives of Fiscal Policy**: The tax structure should facilitate the use of fiscal policy for stabilization and growth by suitably providing for automatic stabilizers as well supporting the saving performance of the economic agents.

5. **Fair Administration**: The tax system should permit a fair, transparent, non-arbitrary, and easily understandable administration for the tax payers.

6. **Minimum Administration and Compliance Costs**: The tax system should involve minimum costs of administration for the government and compliance costs for the tax payer.

For a federal system, there is the additional need to ensure that the principle of correspondence of resources and responsibilities is satisfied. In a federal system, the assignment of resources and responsibilities between the different tiers of government is normally such that the Centre is given relatively larger resources compared to its responsibilities and the States have relatively larger responsibilities compared to the resources assigned to them. This gives rise to vertical imbalance in the system. The vertical
imbalance is brought into balance by a system of transfer of resources from the Centre to the States. It is done in a way such that horizontal imbalance, that is differences in the resource bases and needs of different states is also resolved to the extent possible. Excess vertical imbalance leads to centralization of fiscal space, which is contrary to the idea of federalism. Too little vertical imbalance reduces the centre’s capacity to take care of the horizontal imbalances. Different countries seek a stable solution of establishing the right degree of vertical imbalance given its empirical characteristics. Reform in the indirect tax system has to take into account how the existing relativities of revenues between the Centre and the States would be affected by these reforms.

**1.4 Assignment of Taxes in India**

In this section, we look at the present constitutional scheme relating to taxation of goods and services and recent reforms that have led the system of taxation of goods towards a regime of VAT. In India, taxes have been assigned between the central and the state governments as specified in the Union List and State List in Seventh Schedule of the Constitution. From among the resources assigned to the states, they can assign resources to the local bodies as per the provisions of the 73rd and 74th Amendments to the Constitution. Any unlisted sources of taxation are taxable by the Union government, which has been vested with residuary powers of taxation. Table 1.2 summarizes the constitutional assignment of taxes between the Union and State governments. The main central taxes are personal income tax, corporation tax, Union excise duties (Cenvat), customs duties, and service tax. The main state taxes are sales tax, motor vehicle tax, stamp duty and registration fees, state excise duties, entertainment tax, tax on land and agricultural incomes.

The Constitution, under Articles 268 and 269 makes provision for the assignment of some of the Union taxes to the states for collection and sharing or retaining the amount of revenues raised. The specific provisions are given at Annexure A1. Article 268 refers to taxes levied by the Union but collected and appropriated by the States. Article 269 refers to taxes levied and collected by the Union but assigned to the States.

In a recent Amendment (88th Amendment), the service tax has been brought in under Article 268A. Since the sharing of central taxes with the states under Article 270 provides that taxes under Articles 268/269 are not covered by the provisions of Article 270, service tax revenues have been taken out of the purview of the recommendations of the Finance Commission. In practice, however, a share similar to other central taxes is being
### Table 1.2

**Assignment of Taxes: Union and State Governments**

<table>
<thead>
<tr>
<th>Union Taxes</th>
<th>State Taxes</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Taxes on income other than agricultural income</td>
<td>1. Land revenue, including the assessment and collection of revenue, the</td>
</tr>
<tr>
<td>2. Duties of customs including export duties</td>
<td>maintenance of land records, survey for revenue purposes and records of</td>
</tr>
<tr>
<td>3. Duties of excise on tobacco and other goods manufactured and produced in</td>
<td>rights, and alienation of revenues</td>
</tr>
<tr>
<td>India except –</td>
<td>2. Taxes on agricultural income</td>
</tr>
<tr>
<td>4. Alcoholic liquors for human consumption</td>
<td>3. Duties in respect of succession to agricultural land</td>
</tr>
<tr>
<td>5. Opium, Indian hemp and other narcotic drugs and narcotics but</td>
<td>4. Estate duty in respect of agricultural land</td>
</tr>
<tr>
<td>including medicinal and toilet preparations containing alcohol or</td>
<td>5. Taxes on land and buildings</td>
</tr>
<tr>
<td>any substance included in sub-paragraph (b) of this entry</td>
<td>6. Taxes on mineral rights subject to any limitations imposed by Parliament</td>
</tr>
<tr>
<td>6. Corporation tax</td>
<td>by law relating to mineral development</td>
</tr>
<tr>
<td>7. Taxes on the capital value of the assets, exclusive of agricultural</td>
<td>7. Duties of excise on the following goods manufactured or produced in the</td>
</tr>
<tr>
<td>land</td>
<td>State and countervailing duties at the same or lower rates on similar</td>
</tr>
<tr>
<td>8. Duties in respect of succession to property other than agricultural</td>
<td>goods manufactured or produced elsewhere in India</td>
</tr>
<tr>
<td>land</td>
<td>8. Alcoholic liquors for human consumption</td>
</tr>
<tr>
<td>9. Terminal taxes on goods and passengers, carried by railway, sea or air,</td>
<td>9. Opium, Indian hemp and other narcotic drugs and narcotics, but not</td>
</tr>
<tr>
<td>taxes on railway fares and freights</td>
<td>including medicinal and toilet preparations containing alcohol or any</td>
</tr>
<tr>
<td>10. Taxes other than stamp duties on transactions in stock exchanges and</td>
<td>substance included in sub-paragraph (b) of this entry</td>
</tr>
<tr>
<td>futures markets</td>
<td>10. Taxes on entry of goods into a local area for consumption, use or sale</td>
</tr>
<tr>
<td>11. Rates of stamp duty in respect of bills of exchange, cheques,</td>
<td>therein</td>
</tr>
<tr>
<td>promissory notes, bills of lading, letters of credit, policies of</td>
<td>11. Taxes on the consumption or sale of electricity</td>
</tr>
<tr>
<td>insurance, transfer of shares, debentures, proxies and receipts</td>
<td>12. Taxes on the sale or purchase of goods other than newspapers, subject to</td>
</tr>
<tr>
<td>12. Taxes on the sale and purchase of newspapers and on advertisement</td>
<td>the provisions of entry 92 A of List I</td>
</tr>
<tr>
<td>published therein</td>
<td>13. Taxes on advertisements other than advertisements published in</td>
</tr>
<tr>
<td>13. Taxes on the sale and purchase of goods other than newspapers, where</td>
<td>newspapers and advertisements broadcast by radio or television</td>
</tr>
<tr>
<td>such sale or purchase takes place in the course of inter-state trade</td>
<td>14. Taxes on goods and passengers carried by road or inland waterways</td>
</tr>
<tr>
<td>or commerce</td>
<td>15. Taxes on vehicles, whether mechanically propelled or not, suitable for</td>
</tr>
<tr>
<td>14. Taxes on the consignment of goods (whether the consignment is to the</td>
<td>use on roads, including tramcars subject to the provisions of entry 35</td>
</tr>
<tr>
<td>person making it to or to any other person), where such consignment</td>
<td>of List III</td>
</tr>
<tr>
<td>takes place in the course of the inter-state trade or commerce</td>
<td>16. Taxes on animals and boats</td>
</tr>
<tr>
<td>15. Service Tax</td>
<td>17. Tolls</td>
</tr>
<tr>
<td></td>
<td>18. Taxes on professions, trades, callings and employments</td>
</tr>
<tr>
<td></td>
<td>19. Capitation taxes</td>
</tr>
<tr>
<td></td>
<td>20. Taxes on luxuries, including taxes on entertainments, amusements,</td>
</tr>
<tr>
<td></td>
<td>betting and gambling</td>
</tr>
</tbody>
</table>

**Source:** Constitution of India
given to the states from out of the net proceeds of the services tax. In this context, the Twelfth Finance Commission had observed: “… it is necessary to ensure that the revenue accruing to the states, under the new arrangement should not be less than the share that would accrue to the states, had the entire service tax proceeds been part of the shareable pool”. The changes in respect of Article 268 are summarized in Box 1.

**Box 1: Changes with respect to the Service Tax**

**Insertion of new Article 268A.** - After article 268 of the Constitution, the following article shall be inserted, namely:-

Service tax levied by Union and collected and appropriated by the Union and the States.

“268A. Service tax levied by Union and collected and appropriated by the Union and the States.-(1) Taxes on services shall be levied by the Government of India and such tax shall be collected and appropriated by the Government of India and the States in the manner provided in clause (2).

(2) The proceeds in any financial year of any such tax levied in accordance with the provisions of clause (1) shall be-

(a) collected by the Government of India and the States;

(b) appropriated by the Government of India and the States,

in accordance with such principles of collection and appropriation as may be formulated by Parliament by law.”

3. **Amendment of Article 270.** - In Article 270 of the Constitution, in clause (1), for the words and figures “Articles 268 and 269”, the words, figures and letter “Articles 268, 268A and 269” shall be substituted.

4. **Amendment of Seventh Schedule.** - In the Seventh Schedule to the Constitution, in List I-Union List, after entry 92B, the following entry shall be inserted, namely:-

“92C. Taxes on services.”.

1.5 **Changing Structure of the Indian Economy**

The structure of the Indian economy has been persistently changing in favour of services. In India, the share of the agricultural sector has come down over the years, the share of manufacturing has increased to a limited extent, but the share of the services sector has been increasing steadily. Table 1.3 (Appendix Tables A1 and A3) highlights the changing structure of the Indian economy by looking at the share of GDP at factor cost (1999-00 base series) at current as well as constant (1999-00) prices. The share of agriculture has
come down from more than 55 per cent in 1950-51 to about 18.5 per cent by 2006-07. The share of industry, which was only about 11 per cent of GDP in 1950-51 now accounts for nearly 20 per cent.

Table 1.3
The Changing Sectoral Composition of Indian GDP (1999-00 Base Series)

\[
\begin{array}{|l|c|c|c|c|c|c|}
\hline
& \text{Agriculture and Allied Activities} & \text{Agriculture} & \text{Industry} & \text{Mining and Quarrying} & \text{Manufacturing} & \text{Electricity, Gas and Water Supply} \\
\hline
\text{At Constant (1999-00) prices} & & & & & & \\
1950-51 & 55.28 & 48.36 & 10.65 & 1.42 & 8.92 & 0.31 \\
1960-61 & 50.81 & 45.60 & 13.18 & 1.67 & 10.94 & 0.57 \\
1970-71 & 44.31 & 39.42 & 15.46 & 1.69 & 12.64 & 1.13 \\
1980-81 & 37.92 & 34.37 & 17.45 & 2.01 & 13.82 & 1.61 \\
1990-91 & 31.37 & 28.75 & 19.80 & 2.68 & 14.95 & 2.17 \\
\hline
\text{At Current prices} & & & & & & \\
1950-51 & 52.57 & 49.68 & 11.93 & 0.78 & 10.93 & 0.24 \\
1960-61 & 42.85 & 40.59 & 15.76 & 1.07 & 14.14 & 0.55 \\
1970-71 & 42.40 & 40.14 & 16.32 & 1.08 & 14.19 & 1.04 \\
1980-81 & 35.70 & 32.81 & 20.12 & 1.76 & 16.72 & 1.64 \\
2000-01 & 23.35 & 21.24 & 20.37 & 2.37 & 15.60 & 2.93 \\
2006-07 QE & 18.35 & 16.74 & 20.85 & 2.69 & 16.30 & 1.86 \\
\hline
\end{array}
\]

Source (Basic data): National Income Accounts, CSO.
QE: Quick Estimates

Table 1.4 (Appendix Table A2 and A4) shows the relative shares of key service sectors. The share of services in GDP has increased from nearly 34 per cent in 1950-51 to more than 60 per cent in 2006-07. Not only the service sector has progressively become larger.
but this trend is likely to continue as the service sectors are growing at relatively faster pace, particularly as compared to the agricultural sector. Within the service sector, all the sub groups have consisting of (1) construction, (2) Trade, Hotels, Transport and Communications, (3) Financing, Insurance, Real Estate and Business services, and (4) Community, Social, and Personal Services, have grown. The largest increases seem to have been in construction (nearly four-fold at current prices) and trade, hotel, transport, and communications (the increase at current prices is much more than that at constant prices, indicating the increase in the average prices of these services). The least increase in share is for the community, social, and personal services sector.

Table 1.4
The Changing Composition of the Service Sector in India's GDP
(1999-00 base series)

<table>
<thead>
<tr>
<th>Year</th>
<th>Service (percent)</th>
<th>Construction (percent)</th>
<th>Trade, Hotels, Transport and Communication (percent)</th>
<th>Financing, Insurance, Real Estate and Business services (percent)</th>
<th>Community, Social, and Personal Services (percent)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1950-51</td>
<td>34.07</td>
<td>4.43</td>
<td>11.34</td>
<td>7.69</td>
<td>10.61</td>
</tr>
<tr>
<td>1960-61</td>
<td>36.01</td>
<td>5.58</td>
<td>13.05</td>
<td>7.03</td>
<td>10.35</td>
</tr>
<tr>
<td>1970-71</td>
<td>40.23</td>
<td>6.64</td>
<td>14.74</td>
<td>6.82</td>
<td>12.03</td>
</tr>
<tr>
<td>1980-81</td>
<td>44.63</td>
<td>6.60</td>
<td>17.45</td>
<td>7.49</td>
<td>13.10</td>
</tr>
<tr>
<td>1990-91</td>
<td>48.83</td>
<td>6.12</td>
<td>18.34</td>
<td>10.58</td>
<td>13.78</td>
</tr>
<tr>
<td>2000-01</td>
<td>56.12</td>
<td>5.81</td>
<td>22.30</td>
<td>13.04</td>
<td>14.98</td>
</tr>
<tr>
<td>2006-07 QE</td>
<td>61.94</td>
<td>7.20</td>
<td>26.81</td>
<td>14.32</td>
<td>13.62</td>
</tr>
</tbody>
</table>

At Constant (1999-00) prices

<table>
<thead>
<tr>
<th>Year</th>
<th>Service (percent)</th>
<th>Construction (percent)</th>
<th>Trade, Hotels, Transport and Communication (percent)</th>
<th>Financing, Insurance, Real Estate and Business services (percent)</th>
<th>Community, Social, and Personal Services (percent)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1950-51</td>
<td>35.50</td>
<td>2.58</td>
<td>9.72</td>
<td>12.02</td>
<td>11.18</td>
</tr>
<tr>
<td>1960-61</td>
<td>41.39</td>
<td>3.84</td>
<td>11.64</td>
<td>14.26</td>
<td>11.65</td>
</tr>
<tr>
<td>1970-71</td>
<td>41.28</td>
<td>4.51</td>
<td>12.72</td>
<td>12.05</td>
<td>12.00</td>
</tr>
<tr>
<td>1980-81</td>
<td>44.18</td>
<td>4.57</td>
<td>16.07</td>
<td>10.57</td>
<td>12.97</td>
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<tr>
<td>1990-91</td>
<td>49.21</td>
<td>5.38</td>
<td>18.89</td>
<td>11.62</td>
<td>13.32</td>
</tr>
<tr>
<td>2000-01</td>
<td>56.28</td>
<td>5.82</td>
<td>22.28</td>
<td>13.23</td>
<td>14.94</td>
</tr>
<tr>
<td>2006-07 QE</td>
<td>60.80</td>
<td>8.43</td>
<td>25.05</td>
<td>13.90</td>
<td>13.42</td>
</tr>
</tbody>
</table>

Source (Basic data): National Income Accounts, CSO.
QE: Quick Estimates
1.6 Taxation of Goods in India

a. Central Excise Duties

In this section, we look at the present constitutional scheme relating to taxation of goods and services and recent reforms that have led to the system of taxation of goods towards a regime of VAT.

Union excise duties and cesses are levied on commodities covered by the Central Excise Act, 1944 and the Central Excise Tariff Act 1985. Being an excise duty, this tax captures or uses the valued added up to the stage of manufacturing. The term ‘manufacture’ means bringing into existence a new article having a distinct name, character, use and marketability and includes packing, labeling etc. Most of the products used to attract excise duties at the rate of 14 per cent until recently. As per an announcement in December 2008, the core Cenvat rate has been brought down to 10 per cent. Some products also attract special excise duty/and an additional duty of excise at the rate of 8 per cent above the Cenvat rate. In addition, there is a 2 per cent education and 1 per cent higher education cess applicable on the aggregate of the duties of excise. Excise duty is levied on \textit{ad valorem} basis or based on the maximum retail price in some cases.

The central excise duties have historically been an important tax on the manufacture or production of domestic goods. Since the late eighties, these excise duties have been transformed as taxes levied under the value-added principle going up to the manufacturing or production stage. It was first transformed into what was called a Modified Value Added Tax (Modvat) and later as Central Value Added Tax (Cenvat) in the latter part of the nineties.

The Modvat was introduced in the 1986-87 Budget. With effect from March 1, 1986, a proforma credit scheme was extended to products with reference to specified Chapters of the Central Excise Tariff Act, 1985. A major objective of the Modvat scheme was to initiate a system of taxation, which can reduce cascading of taxes, and thereby also reduce costs and prices. At first, the coverage was limited to 37 out of 91 Chapters. With effect from March 1, 1987, all commodities except petroleum products, textiles, tobacco, cinematographic films and matches were covered. In the Modvat system, early in the nineties, full rebate on the excise tax paid on capital goods was allowed instead of setting up a system of annual depreciation related deductions. With effect from 1995-96, the entire manufacturing chain was brought under Modvat. In the 2000-01
central budget, the excise deduction on capital goods was permitted to be spread over two years.

In the late nineties, the Modvat system was renamed as Cenvat, which had fewer rates. In view of revenue and equity considerations, a few higher rates for demerit goods like tobacco products (cigarettes, cigars, chewing tobacco or mixed in pan masala) and for final, finished, luxury consumer durable goods like cars were considered justifiable.

The general highlights of Cenvat scheme may be described as follows. The Cenvat scheme is based on the system of granting credit of duty paid on inputs and input services. A manufacturer or service provider has to pay excise duty and service tax as per normal procedure on the basis of ‘assessable value’. However, he gets credit of duty paid on inputs and service tax paid on input services. Credit is made available of excise duty paid on (a) raw materials (excluding few items) (b) material used in or in relation to manufacture like consumables etc. and (c) paints, packing materials, fuel etc. used for any purpose. However, duty paid on high speed diesel oil (HSD), light diesel oil (LDO) and motor spirit (petrol) is not available as Cenvat credit, even if these are used as raw materials or as fuel.

No credit is available if final product is exempt from duty or final service is exempt from service tax. If a manufacturer manufactures more than one product, it may happen that some of the products are exempt from duty. Similarly, in case of service provider, some services may be taxable while some services may not be covered. In such cases, duty paid on inputs and service tax paid on input services used for manufacture of exempted products/services cannot be used for payment of duty or tax on other final products/services which are not exempt from the tax. In case of exempt services, he can utilise Cenvat credit only up to 20 per cent of service tax payable on output service. Cenvat credit does not require a one-to-one correspondence or input-output correlation. In the case of capital goods credit of duty paid on machinery, plant, spare parts of machinery, tools, dies, etc., is available up to 50 per cent in the current year and balance in subsequent financial year or years.

In 2005, the core Cenvat rate was kept at 16 per cent for a majority of the items. There were two more rates: 24 per cent and 8 per cent. Effectively, there were several other rates of excise duty that continue to be applied on different items, subject to their end-use. With the 2008-09 budget, the core Cenvat rate was brought down to 14 per cent. This has now been brought down to 10 per cent but still multiple rates exist. In addition
to the Cenvat, several cesses and surcharges and additional levies are used. These are listed below:

a) Special Excise Duty: Special excise duty is leviable by the Central Excise Tariff Act, 1985.

b) National Calamity Contingent Duty: NCC Duty was levied on pan masala and certain specified tobacco products vide the Finance Act, 2001. The Finance Act, 2003 extended this levy to polyester filament yarn, motor car, two wheeler and multi-utility vehicle @ 1 per cent; and (b) crude petroleum oil @ Rs. 50 per metric tonne. In this year’s budget NCCD has been removed from Polyester Filament Yarn and imposed on Mobile Phones @1 per cent.

c) Education Cess: Education Cess is leviable @2 per cent on the aggregate of duties of Excise.

d) Secondary and Higher Education Cess: Leviable @1 per cent on the aggregate of duties of Excise.


f) Cess on High Speed Diesel Oil: Cess on High Speed Diesel Oil is leviable by the Finance Act, 1999.

g) Surcharge on Motor Spirit: Surcharge on Motor Spirit is leviable by the Finance Act, 2002.

h) Surcharge on Pan Masala and Tobacco Products: An Additional Duty of Excise has been imposed on cigarettes, pan masala and certain specified tobacco products, at specified rates in the Budget 2005-06. Biris are not subjected to this levy.

b. Customs Duties

The customs duties are levied on imports brought into the country. These are not part of taxation of domestic value added but contain some element to bring the tax treatment of foreign producers in the matter of taxation of goods on par with domestic producers. The customs duty in India consists of ‘basic’ tariff, the Additional Duty of Customs (AD), and Special Excise Duty (SAD). The additional duty is the counterpart of excise duties paid by domestic manufacturers i.e. Countervailing Duty (CVD). The special excise duty
has been introduced to serve as the counterpart of state sales taxes on domestically produced goods. The customs duty is thus collected under the three sub-heads (basic, AD and SAD).

In addition to the basic customs duty, several surcharges and cesses are also leviable as given below.

a) Additional Duty of Customs (CVD): Additional Duty of Customs is leviable under Section 3 of the Customs Tariff Act, 1975 equivalent to duty of Central Excise leviable on such domestically manufactured goods.

b) Special CV Duty: Special CV Duty is leviable @ 4% on all imported goods, with few exceptions, to partially compensate the domestic levies.


d) Cess on High Speed Diesel Oil: Cess on High Speed Diesel Oil is leviable by the Finance Act, 1999.


f) National Calamity Contingent Duty: This duty was imposed under Section 134 of the Finance Act, 2003 on imported petroleum crude oil. This tax was also leviable on motor cars, imported multi-utility vehicles, polyester filament yarn and two wheelers.

g) Education Cess: Education Cess is leviable @ 2 per cent on the aggregate of duties of Customs (except safeguard duty under section 8B and 8C, CVD under section 9 and anti-dumping duty under section 9A of the Customs Tariff Act, 1985). Items attracting customs duty at bound rates under international commitments are exempted from this cess.

h) Secondary and Higher Education Cess: Leviable @1 per cent on the aggregate of duties of customs.

c. State Sales Tax

State taxes include state sales taxes, the Central Sales Tax (CST) assigned by the Central Government to the states, motor vehicle tax, state excise duties, entertainment taxes, and other taxes as indicated in Table 1.2. The Constitution empowers the states to levy ‘taxes
on sale or purchase of goods other than newspapers, subject to provisions of entry 92 A of List I. This entry provides that the Central Government is empowered to levy a tax on the sale and purchase of goods other than newspapers where such sale or purchase takes place in the course of inter-State trade or commerce. The Central Government has levied a central sales tax on inter-State sales, which under Article 269, is collected and retained by the states.

The structure of sales tax, prior to reforms undertaken in late nineties was characterized by high tax rates, multiplicity of tax rate and exemptions, lack of uniformity across states, large number incentives, and cascading of taxes. During reforms of sales taxes prior to the introduction of state VAT, most states had agreed to phase out the incentive related exemptions, and implement floor rates. There are several minor taxes imposed by the States on the sale, purchase, storage and movement of different goods.

Sales taxes are normally levied at the point of sale to the consumer. In India, however, states had followed the practice of “first point sales tax,” where the tax is collected at the point of sale by the producer. In such a system, the tax was not levied on all the stages of value addition or sales and distribution channel. The margins of distributors/dealers/retailers were not subject to sales tax. As such, the single-point levy had to be at a high rate to cover the value added at all stages. The high rate structure led to the need for a highly differentiated rate structure and exempted categories, which led to various classifications disputes and tax evasion. Apart from the general sales tax, most states levied an additional sales tax or a surcharge. In addition, the states levy luxury tax as also an entry tax on the sale of imported goods.

All these practices led to heterogeneity in structure, as well as rates, causing diversion of trade as well as shifting of manufacturing activity from one State to another. Further, widespread taxation of inputs led to vertical integration of firms, encouraging production of more and more of the inputs needed rather than purchasing them from ancillary industries. This system taxation of goods became non-neutral, interfering with the producers’ choice of inputs as well as with the consumers’ choice of consumption, thereby leading to severe economic distortions.

With the initiative of Empowered Committee of the State Finance Ministers, states initiated indirect tax reforms in the late nineties. As a first step, they reduced the rate categories in the case of sales taxes, reduced exemptions, and introduced floor rates.
There were tangible revenue benefits after these changes, which facilitated, under the guidance of the Empowered Committee, the implementation of state level VAT.

The State-VAT recommended by the Empowered Committee of State Finance Ministers was elaborated in a White Paper brought out by the Government of India. The State-VAT provides full set-off for input tax as well as tax on previous purchases. It also abolished the burden of several of the existing taxes, such as turnover tax, surcharge on sales tax, additional surcharge, special additional tax, etc. The CST however continues although its rate has been progressively brought down. The main features of the scheme suggested by the Empowered Committee were:

a. uniform schedule of rates of VAT for all states, making the system simple and uniform and prevent unhealthy tax competition among states;
b. the provision of input tax credit meant for preventing cascading effect of tax;
c. the provision self assessment by dealers aimed at reducing harassment; and
d. the zero rating if exports aimed at increasing the competitiveness of Indian exports.

As per the basic principles of VAT, the State-VAT provides that for all exports made out of the country, tax paid within the state will be refunded in full. Units located in Special Economic Zone (SEZ) and Export Oriented Units (EOUs) are to be granted either exemption from payment of input tax.

In the original proposal registration of dealers with gross annual turnover above Rs. 5 lakh was made compulsory. There was a provision for voluntary registration with flexibility given to the states to fix their own threshold limits. Small dealers with annual gross turnover not exceeding Rs. 50 lakh who are otherwise liable to pay VAT, may be given the option for a composition scheme with payment of tax at a small percentage of gross turnover. The dealers opting for this composition scheme will not be entitled to input tax credit. For better inter-State coordination, the Empowered Committee has suggested that there should be a Tax Payer's Identification Number, which will consist of 11 digit numerals throughout the country.

The basic simplification of the State-VAT is that VAT liability is self-assessed by the dealers themselves in terms of submission of returns upon setting off the tax credit. In the State-VAT scheme, all the goods, including declared goods are to be covered and get the benefit of input tax credit. The few goods outside the VAT are liquor, lottery tickets,
petrol, diesel, aviation turbine fuel and other motor spirit since their prices are not fully market determined. These will continue to be taxed under the Sales Tax Act or any other State Act or even by making special provisions in the VAT Act itself, and with uniform floor rates decided by the Empowered Committee.

The most important part of the VAT scheme relates to the tax rates. Under the VAT system covering about 550 goods, only two basic VAT rates of 4 and 12.5 per cent are to apply plus a specific category of tax-exempted goods and a special VAT rate of 1 percent only for gold and silver ornaments.

Under the exempted category, the Empowered Committee placed 46 commodities comprising of natural and unprocessed products in the un-organized sector, items that are legally barred from taxation and items which have social implications. Under the State-VAT, there is the proposal to give flexibility to the states to select a set of maximum of 10 commodities States for exemption from a list of goods specified by the Empowered Committee, which are of local social importance for the individual States without having any inter-State implications.

The rest of the commodities in the list are common for all the States. Under 4 percent VAT rate category, the largest number of goods (about 270) were placed, common for all the States, comprising of items of basic necessities such as medicines and drugs, all agricultural and industrial inputs, capital goods and declared goods. The remaining commodities, common for all the States, will fall under the general VAT rate of 12.5 per cent.

It was proposed that VAT on AED items relating to sugar, textile and tobacco, because of initial organizational difficulties, will not be imposed for one year after the introduction of VAT and till then the existing arrangement will continue.

Table 1.5 indicates the sequence in which the states joined the State-VAT scheme. Five states implemented VAT in 2006-07. Tamil Nadu and Uttar Pradesh were the last to join the VAT system. The States had already taken measures to streamline the procedures, rationalize tax rates and address other issues so as to enable a smooth transition to VAT in their respective States. State Governments in general have aimed at expanding the tax payer base, better compliance, rationalization of tax rates, improving the efficiency of tax administration, simplification of tax laws and introducing a modern and improved tax system. Excepting for a few States which have contemplated to bring in new taxes (tax on
lottery tickets in Maharashtra, tax on resale of certified used cars in Goa, ‘green tax’ on old vehicles in Rajasthan), most State Governments have intended to reduce their tax rates on various types of taxes and even abolish certain taxes. In this context it may be mentioned that two States (Punjab and Maharashtra) have shown inclination to do away with Octroi. Kerala, on the other hand, has created a new schedule of goods to be taxed at 20 per cent which is higher than the highest level under VAT i.e., 12.5 per cent.

Table 1.5
Implementation of Value Added Tax by States

<table>
<thead>
<tr>
<th>States</th>
<th>Month and Year</th>
<th>States</th>
<th>Month and Year</th>
</tr>
</thead>
<tbody>
<tr>
<td>15. Maharashtra</td>
<td>April 2005</td>
<td></td>
<td></td>
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</tbody>
</table>

Source: RBI, Based on Information received from the State Governments.

The Empowered Committee emphasized the phasing out of Central Sales Tax (CST) after introduction of VAT. State were collecting nearly Rs. 15 thousand crore every year from CST when the rate was 4 per cent. The Central Government has reduced the rate first to 3 per cent and now to 2 per cent and agreed to give the states some compensation. As CST is phased out, there is also a critical need for putting in place a regulatory frame-
work in terms of Taxation Information Exchange System to give a comprehensive picture of inter-State trade of all commodities. This process of setting up of Taxation Information Exchange System has already been started by the Empowered Committee.

Under exempted category, the Empowered Committee suggested that about 46 commodities comprising of natural and unprocessed products in the un-organized sector, items that are legally barred from taxation and items which have social implications should be included with a flexibility to the states to select a set of maximum of 10 commodities States for exemption goods of local social importance for the individual States without having any inter-State implications.

Under 4 per cent VAT rate category, items of basic necessities such as medicines and drugs, all agricultural and industrial inputs, capital goods and declared goods are to be included. The remaining commodities, common for all the States, will fall under the general VAT rate of 12.5 per cent.

Notwithstanding the guidelines given by the Empowered Committee, in terms of actual implementation, considerable variation developed across states. Most states have divided the goods taxable at different rates into several schedules. We consider a set of selected states to highlight some of the differences in the way that the goods are being classified in the states. For example, in Tamil Nadu, there are six separate schedules, which contain different parts. In the first schedule, part A relates to goods which are taxable at the rate of one per cent. These include bullion, gold, silver and precious stones. Part B of the first schedule lists goods that are taxable at the rate of 4 per cent. This list includes 150 items. Part C of the first schedule includes the residual category of goods which are taxable at the rate of 12.5 per cent. The second schedule includes goods where there is no entitlement for input tax credit. These include alcoholic liquors, gasoline, petrol and high speed and diesel oil, kerosene other than those sold through the PDS, molasses, and sugarcane. The rates vary very widely among these goods from 4 per cent to 73 per cent. The third schedule provides for compounded rates for hotels, restaurants and sweet stalls. The fourth schedule gives a list of goods exempted from the state VAT under two parts, part A and part B. Part A contains 10 goods and part B contains 81 goods. The fifth and sixth schedules relate to international organizations where sale is zero-rated and where a transit pass is permissible, respectively.

In the case of Andhra Pradesh, there are six schedules. However, these are quite differently organized compared to Tamil Nadu. Schedule 1 provides a list of exempted goods which
are about 47 in number. Schedule 2 provides a list of zero rated goods that are eligible for input tax credit. Schedule 3 provides a list of credits that are taxable at 1 per cent rate and include bullion, jewellery and precious stones. Schedule 4 provides a list of goods that are taxable at 4 per cent. The list contains 90 items. Schedule 5 is the residual category of goods where the rate of 12.5 per cent applies. Schedule 6 includes goods subjected to tax at special rates including liquor, petrol, aviation motor spirit, aviation turbine fuel and diesel oil. These are levied at first point sales and range from 21.33 per cent to 90 per cent. However, in the case of Andhra Pradesh, input tax credits for these items in schedule 6 have been provided for.

In the case of Punjab VAT schedules have been divided into 8 categories and the schedules range from A to H. Schedule A contains the list of exempted goods. These are 65 in number. Schedule B contains goods taxable at 4 per cent and these are 149 in number. Liquor is included in this list. Schedule C contains goods taxable at one per cent covering bullion etc. Schedule D contains only one item, viz., aviation turbine fuel taxable at the rate of 20 per cent. No input tax credit is provided in respect of purchases of petrol, diesel, aviation turbine fuel, liquefied petroleum gas, and condensed natural gas. This is also applicable for beverages and tobacco products. Schedule E provides a list of goods taxable at special rates. This includes only three items viz., diesel, molasses and petrol and the tax rates vary from 8.8 per cent for diesel to 27.5 per cent for petrol. Schedule F is the residual category where goods are taxable at 12.5 per cent. Schedule G makes reference to the UN bodies and Schedule H provides a list of good on which VAT is levied on the taxable turnover. These include paddy, wheat, cotton, sugarcane and milk.

For Maharashtra, there are five schedules. Schedule A gives a list of exempted goods. These are 54 in number and include electricity. Schedule B refers to the tax rate of one per cent applicable on gold, silver and precious metals. Schedule C gives the list of goods that are taxes at 4 per cent. In this list, 109 groups of goods are mentioned. These include iron and steel, various metals, lime and lime stone and their products, paper, and plastic granules etc. Schedule D includes goods taxed at 20 per cent or above. Foreign and country liquor and molasses and spirit are taxed at 20 per cent. For high speed diesel oil, aviation turbine fuel, aviation gasoline and motor spirit the rates vary between 27 to 34 per cent with a specific component added amounting to Re. 1 per litre in most cases. Schedule E is the residual category taxed at 12.5 per cent. A distinction is made according to whether the dealer is located in Brihan Mumbai, Navi Mumbai or Thane and a dealer located elsewhere in Maharashtra.
In the case of Delhi, there are 7 schedules. Schedule 1 gives the list of exempted commodities which includes electricity and energy, rubber and plastic footwear and plastic waste. Schedule 2 is for the 1 per cent rate relating to gold, and precious metals. Scheduled 3 include goods that are taxed at 4 per cent. This includes 84 items that covers industrial cables and ferrous and non ferrous metals, paper and news print, pipes and plastic footwear, and plastic granules, powder and master batches. It also includes cooper and various other metals and carbon. It also includes insecticides, fungicides and pesticides of technical grade, and various industrial inputs. Schedule 4 provides a list of goods taxed at 20 per cent. It includes petroleum products other than liquid petroleum oil, naphtha, aviation turbine fuel, spirit, gasoline, liquor including country liquor and molasses among others. The 5th and 6th schedules give the list of various categories of dealers and organizations who are exempted on paying tax on sale of goods. The 7th schedule provides a list of non creditable goods. This includes all automobiles including commercial vehicles, and two and three wheelers, fuels in the form of petrol, diesel, LPG, CNG and coal, beverages for human consumption, air conditioners, tobacco etc. The residual category of goods where the tax rate is 12.5 per cent is not separately mentioned and is included in Chapter 2, clause 4 of the Act.

It is clear that while there is some uniformity in the tax rates which range from exempted goods, zero rated goods (for exports), goods taxed at one per cent, goods taxed at 4 per cent, and goods taxed at 12.5 per cent, there is considerable variation among the states regarding the goods included in different categories. There are also several goods where special rates are applied and these rates vary considerably across states. There is also considerable variation in the list of goods subject to special rates where credit on taxes paid on goods is allowed or not allowed. Many goods that may be considered as polluting inputs and outputs are taxed at different rates in the states. With a view to deriving a broad idea of such differences, we consider the state-wise treatment of a selective list of these goods which may be considered prima-facie as polluting inputs and outputs.

d. Other State Taxes on Goods and Services

Motor Vehicle Tax

In most states a compounded system of motor vehicle tax exists, where a one time levy is paid for the life of the vehicle. This may be useful, particularly if the tax payers are to be saved from the hassle of interacting with the tax department every year. However,
compounded levies are neither revenue productive nor do they permit additional taxation when vehicles become less efficient and more polluting.

**Stamp Duty and Registration Fees**

The stamp duty on the registration of property or other conveyances has the main difficulty of getting the correct method of evaluation. Until recently, the stamp duty rates were excessively high in most states and the procedures for evaluating the conveyances were also complicated. In recent years, states have undertaken reforms by reducing the duty rates and streamlining procedures for evaluation of property. There has been an attempt to move towards uniform stamp duty rates. While in Punjab it is 6 per cent, in Himachal Pradesh, there is a 12 per cent duty, Uttar Pradesh 10 per cent and Rajasthan 11 per cent. The Union finance ministry has asked states to adopt a uniform 5 per cent stamp duty. Following this, some states like Maharashtra and Bihar went for a reduction in existing stamp duties. In 2002, Delhi cut stamp duty rates from 13 per cent to 8 per cent for men registering property and brought it down to 6 per cent for women owners. In case of joint ownership by men and women, the duty is 7 per cent. In Delhi, stamp duty rates were further reduced for women at 4 per cent against 6 per cent for men. Recently, Haryana reduced stamp duty for women to 8 per cent while that for men in the state is 10 per cent.

**State Excise Duties**

The power of states to levy excise duties is limited to alcoholic liquors for human consumption, and opium, Indian hemp and other narcotic drugs excluding those used for medicinal purposes or for toilet preparations. The revenues accrue to the states in the form of licence duties from the vendors as well as the tax, which can be specific or ad valorem. Consumption of alcohol and other beverages containing spirit are known to be hazardous and injurious to health. The Constitution has provided the State governments with a monopoly to tax the production and sale of alcoholic beverages. The State governments also control the production of these by giving licenses and often specifying the quantity to which the production should limited. Since demand for alcoholic beverages is generally assessed to be price-inelastic, this tax provides a case for keeping high tax rates for controlling the level of consumption. In fact high tax rates yield both high revenues and greater control on consumption. Some states have from time to time embarked upon the path of total prohibition. Attempts at full prohibition often lead to illegal production and export of the tax base to the neighboring states. Production of alcoholic beverages involves considerable pollution due to the effluents that are discharged.
Electricity Duty

Electricity duty is charged to consumers along with the electricity tariffs or rates. The rates are meant for electricity boards or the providers of electricity, while the electricity duty is meant for the State government. The State government administers the electricity prices, and often owes to the electricity boards payments on account unpaid but committed subsidies. In actual practice, as State governments are unable to pay the requisite amounts due to electricity boards, the boards in turn collect the electricity duty but do not pass these on to the State government. In most states, electricity prices are now regulated by the Electricity Regulatory Authorities but the State governments have a large say in the determination of these prices.

Entertainment Tax

The entertainment tax is a levy on admission to places of amusement or entertainment including cinema, circus, theatrical performances, exhibitions, etc. The entertainment tax is used to be an important source of revenue for the states, but has lost its importance in recent times due to proliferation of means of home-based entertainment, which has also made it difficult to revise tax rates.

e. Local Taxes

The resources of the local bodies, i.e., Panchayats and Municipalities include assignment of land tax, profession tax and surcharge/cess on state taxes in addition to property tax/house tax, octroi/entry tax, and other user charges.

Land taxes: In many States, land revenue has either been abolished or land holdings up to a certain size have been exempted.

Property/House tax: Property tax/house tax is the single most important local tax in a majority of the States. However, it has been beset with a variety of problems that have prevented the local bodies to exploit its full potential. In most States, the tax rates have not been revised periodically and there is no standard mechanism for determination of property tax rates and their revision. One major impediment to the growth of revenue from the property/house tax has been the rent control laws.

Octroi/Entry tax: Besides the property/house tax, octroi has been the major source of revenue for the municipalities and, in some States, even for the panchayats. Many States have, however, abolished octroi with a view to removing impediments to the physical
movement of goods, though several other new barriers have been created. Some States have introduced a levy in lieu of octroi, an entry tax, the net proceeds of which are transferred to the local bodies in the form of grant.

1.7 Taxation of Services

A service tax was levied by the Central government under its residuary powers, as the subject has not been mentioned in any of the Lists of the Seventh Schedule of the Constitution. The service tax was brought into force with effect from 1st July 1994. Initially three services were notified: (1) Telephone (2) Stockbroker, and (3) General Insurance. The Finance Act (2) 1996 enlarged the scope of levy of Service Tax covering three more services, viz., (4) Advertising agencies, (5) Courier agencies, and (6) Radio pager services.

The Finance Acts of 1997 and 1998 further extended the scope of service tax to cover a larger number of services rendered by the following service providers, from the dates indicated against each of them:


The services provided by goods transport operators, out door caterers and pandal shamianna contractors were brought under the tax net in the Budget 1997-98, but abolished vide Notification No.49/98, 2nd June, 1998. Twelve new services were notified on 7th October, 1998 and were subjected to levy of Service Tax w.e.f. 16th October, 1998. These are:

The ambit of the services tax was steadily increased in successive budgets as summarized below.


**Budget 2002-2003:** (42) Auxiliary services to life insurance, (43) Cargo handling, (44) Storage and warehousing services, (45) Event management, (46) Cable operators (47) Beauty parlours, (48) Health and fitness centres, (49) Fashion designer, (50) Rail travel agents, and (51) Dry cleaning services.

**Budget 2003-04:** (52) Commercial vocational institute, coaching centres and private tutorials, (53) Technical testing and analysis (excluding health and diagnostic testing) and technical inspection and certification service, (54) Maintenance and repair services, (55) Commission and installation services, (56) Business auxiliary services, namely business promotion and support services (excluding on information technology services), (57) Internet café, and (58) Franchise services.

**Budget 2004-05:** (59) Transport of goods by road (earlier Goods Transport Operators service re-introduced), (60) Out door caterer’s service (re-introduced), (61) Pandal or Shamiana service (re-introduced), (62) Airport services, (63) Transport of goods by air services, (64) Business exhibition services, and (65) Construction services in relation to commercial or industrial building construction services in relation to commercial or industrial building.

**Budget 2005-06:** (66) Intellectual property services, (67) Opinion poll services, (68) TV or radio programme services, (69) Survey and exploration of minerals services, (70) Travel agent’s services other than rail and air travel agents, (71) Forward contract services, (72) Transport of goods through pipe line or other conduit services, (73) Site preparation and clearance services, (74) Dredging services, (75) Survey and mapmaking services, (76) Cleaning services, (77) Membership of clubs and associations, (78) Packaging services, (79) Mailing list compilation and mailing services, and (80) Construction services in relation to residential complexes.

**Budget 2006-07:** (81) ATM operations, maintenance and management; (82) registrars,
share transfer agents and bankers to an issue; (83) sale of space or time, other than in the print media, for advertisements; (84) sponsorship of events, other than sports events, by companies; (85) international air travel excluding economy class passengers; (86) container services on rail, excluding the railway freight charges; (87) business support services; (88) auctioneering; (89) recovery agents; (90) ship management services; (91) travel on cruise ships; and (92) public relations management services.

**Budget 2007-08:** (93) Services outsourced for mining of mineral, oil or gas; (94) renting of immovable property for use in commerce or business; however, residential properties, vacant land used for agriculture and similar purposes, land for sports, entertainment and parking purposes, and immovable property for educational or religious purposes will be excluded; (95) development and supply of content for use in telecom and advertising purposes; (96) asset management services provided by individuals; (97) design services, and (98) on services involved in the execution of a works contract (an optional composition scheme under which service tax will be levied at only 2 per cent of the total value of the works contract).

**Budget 2008-09:** (99) asset management service provided under ULIP, will be on par with asset management service provided under mutual funds; (100) services provided by stock/commodity exchanges and clearing houses; (101) right to use goods, in cases where VAT is not payable; and (102) customised software, to bring it on par with packaged software and other IT services.

The service tax rate was also progressively increased. It was increased from 5 to 8 per cent on all the taxable services w.e.f. 14.5.2003. It was then enhanced to 10 per cent from 8 per cent in September 2004. Besides this 2 per cent education cess on the amount of service tax was introduced. Subsequently the secondary and higher education surcharge of 1 per cent was also added. Currently the effective service tax rate is 12.36 per cent including education cess.

The main services that have proved to be revenue productive in the case of service are telephones, insurance, brokerage, advertising, courier services, air travel agent services, clearing and forwarding agent services, banking and other financial services, and port services.
1.8 Conclusion

Taxation of goods and services in India has been subject to multiplicity of taxes, large number of cesses and surcharges, cascading, distinction between goods and services and excessive rate categories among the goods, overlapping of taxation space between the Central and State governments in the case of goods up to the stage manufacturing, artificial segmentation of the value added in the process of production and sale between manufacturing and beyond up to the retail space. Such a system did not meet the first principles of a good tax system and several reforms were initiated to bring about a system of value added taxation. In spite of these reforms various problems remain. The system of VAT is at present segmented between Cenvat, State-VAT, the central service tax, and a variety of other taxes at the state level. In all cases, multiple tax rates and a variety of exemptions apply and cascading continues between different taxes. The next chapter discusses the problems arising out of the present system of taxation of goods and services in India after the introduction of the value added tax system.
Continuing Challenges in the Fragmented VAT Systems

2.1 Introduction

In spite of reforms, the system of taxation of goods and services in India falls short of international norms and practices in many developed and developing countries. The main problems relate to issues in defining manufacturing, fragmentation of space of taxation of valued added, issues relating inter-State trade, and the overarching nature of many services that cross state borders in the stages from production to final consumption. India’s problems are particularly challenging because of the federal structure of government. The next logical step is to continue with reforms so as to bring about a comprehensive system of taxation of goods and services consistent with the needs of a modern and efficient economy while preserving the basic features of our federal arrangements. For this purpose, we need to identify the main deficiencies and challenges of the current system, even after nearly two decades of reforms including the introduction of Cenvat and State-VAT. In this Chapter, we examine the continuing problems and the need for further reforms to bring about a comprehensive GST.

2.2 Taxation at Manufacturing Level

The Cenvat is levied on goods manufactured or produced in India. This gives rise to definitional issues as to what constitutes manufacturing, and valuation issues for determining the value on which the tax is to be levied. Manufacturing itself is a narrow base. Limiting the tax to the point of manufacturing is a severe impediment to an efficient and neutral application of tax. The definition of manufacturing and the methodology of valuation have evolved through judicial rulings. The effective burden of tax becomes dependent on the supply chain, i.e., the taxable value at the point of manufacturing relative to the value added beyond this point. It is for this reason that most countries have abandoned this form of taxation and replaced it with multi-point taxation system covering valued added up to the retail level.

a. Concept of Manufacture

The central excise duty, now known as, Central Value Added Tax (CENVAT) is levied on the manufacture and production of ‘excisable goods’ in India. Excise duty may be levied
and collected on goods only if (a) the goods are manufactured, and (b) the goods are marketable. The task of determining what is ‘manufacture’ has led to various disputes and the Courts have often clarified, from time to time, as to what should be considered as manufacture for the purpose of central excise duty.

The Supreme Court of India in the case of Union of India vs. Delhi Cloth & General Mills Co. Limited, held that the word ‘manufacture’ is generally understood to mean “as bringing into existence a new substance” and does not merely mean “to produce some change in substance”. Later, the Supreme Court further clarified the meaning of the term ‘manufacture’ in the case of South Bihar Sugar Mills Ltd vs. Union of India. The Court held:

“The word “manufacture” implies a change but every change in the raw material is not manufacture. There must be such a transformation that a new and different article must emerge having a distinctive name, character or use.”

In a recent judgment, the Supreme Court, in the case of Kores India Ltd., Chennai vs. Commissioner of Central Excise, defined the concept of manufacture as follows: “… manufacture is the end result of one or more processes through which the original commodities are made to pass… There may be several stages of processing, a different kind of processing at each stage. With each process suffered the original commodity experiences a change. Whenever a commodity undergoes a change as a result of some operation performed on it or in regard to it, such operation would amount to processing of the commodity. But it is only when the change or a series of changes takes the commodity to the point where commercially it can no longer be regarded as the original commodity but instead is recognized as a new and distinct article that a manufacture can be said to take place. … (See Collector of Central Excise, Jaipur vs. Rajasthan State Chemical Works, Deedwana, Rajasthan (1891 (4) SCC 473).”

The Court quoted with approval a passage appearing in Volume 26 of the Permanent Edition of the “Words and Phrases” as below:

“Manufacture’ implies a change but every change is not manufacture and yet every change of an article is the result of treatment, labour and manipulation. But something more is necessary and there must be transformation: a new and different article must emerge having a distinctive name, character or use”.

“In our view, the gas generated by these concerns is kiln gas and not carbon dioxide as known to the trade, i. e., to those who deal in it or who use it. The kiln gas in question therefore is neither carbon dioxide nor compressed carbon dioxide known as such to the commercial community and therefore cannot attract Item 14-H in the First Schedule.”
Thus, for consideration as ‘manufacture’, the process involved must bring about a transformation and as a result of such transformation a new and different commercial article must emerge having a distinctive name, character and use. A mere change of form, shape or size of the same article or substance would not ordinarily amount to manufacture.

The definition of manufacture in the Excise Act underwent various Amendments in years 1986, 1999, 2002 and 2003. As a result, ‘manufacture’ was defined to include any process, which is specified as amounting to manufacture in relation to any goods in the Section or Chapter Notes specified in the First Schedule to the Central Excise Tariff Act, 1985 and in respect of goods specified in the Third Schedule to the Excise Act which involve packing or re-packing of such goods in the unit container or labeling or re-labeling of containers including the declaration or alteration of retail sale price on it or adoption of any other treatment on the goods to render the product marketable to the consumer. Thus, by a ‘legal fiction’, certain processes have been equated with manufacture, even though as a result of such processes no new or different article emerges having a distinctive name, character or use.

b. Concept of Goods and Marketability

The second main issue is about valuation. Technically, the manufacturing process may be complete but unless the good enters a market and faces a buyer, there is no value that can be attached to the product. Excise duty, as provided under Section 3 of the Excise Act, is levied on the manufacture or production of ‘excisable goods’. In several judgements, the Supreme Court has held that in order to be goods, an article must be something which can ordinarily come to the market and is brought for sale and must be known to the market as such. Therefore, the essentiality of the concept of marketability is that the goods manufactured are known in the market or are capable of being sold and purchased in the market.

Several cases judgments have clarified this concept. In the case of Union of India vs. Delhi Cloth & General Mills Co. Limited, the assessee was manufacturing hydrogenated vegetable oil (vanaspati). During the process of manufacture, at an intermediate stage, refined oil came into existence. It was the contention of the Revenue Authorities that excise duty was leviable on such refined oil. The assessee contended that the refined oil that came into existence was not refined oil as known to the market since refined oil as known to the market must have undergone the process of deodorisation and that, in their case, the refined oil had not undergone such process. The Supreme Court held that to
become “goods” an article must be something which can ordinarily come to the market to be bought and sold and that since the refined oil, in the condition in which it came into existence in the assessee's factory, was not refined oil which could ordinarily come to the market to be bought and sold, that the said refined oil was not ‘goods’.

c. Classification of Goods

A third problem arises because there is a need to classify the goods so as to determine the appropriate level of duty in a highly differentiated system of levy. It is often not possible to identify all the goods individually. Often the goods are identified through groups and sub-groups and then to determine the rate of duty on each group or sub-groups of goods. For the purposes of classifying goods under various heads and/or sub-heads, Parliament has passed the Central Excise Tariff Act, 1985. The Tariff Act is based on the International Convention of Harmonised System of Nomenclature (HSN).

The First Schedule of the Tariff Act is divided into 20 Sections, which broadly cover separate categories of goods. For instance, Section I deals with live animals: animal products; Section II deals with vegetable products; Section XI deals with textile and textile articles; and Section XV deals with base metals and articles of base metal. Each Section contains a number of Chapters. The First Schedule comprises 96 Chapters.

The Sections and Chapters contain elaborate sections and/or chapter notes. The Tariff Act also contains Rules for the Interpretation of the First Schedule. In spite of these provisions being quite elaborate, they are not always adequate to correctly classify a product. As a result, Courts and Tribunals had to evolve rules over the years for the classification of the products.

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1 In the case of South Bihar Sugar Mills Ltd vs Union of India, the assessee manufactured sugar. During the process of manufacture of sugar, a gas known as ‘kiln gas’ emerged as a byproduct and was released to the atmosphere. The Revenue Authorities sought to levy excise duty on the said kiln gas on the ground that it was either carbon dioxide or compressed carbon dioxide. The contention of the assessee was that kiln gas was not carbon dioxide as known to the market or to the commercial community dealing in carbon dioxide. The Supreme Court held that excise duty is levied on goods and as the Act does not define ‘goods’, the legislature must be taken to have used that word in its ordinary, dictionary meaning. The dictionary meaning is that to become goods it must be something which can ordinarily come to the market to be bought and sold and is known to the market. Looking at the evidence on record the Court held:

“Thus, before excise duty can be levied and collected on any goods, the twin tests of manufacture and marketability have to be satisfied. The burden of proving that goods satisfy the twin tests lies on the Revenue Authorities”.
d. Valuation

The next problem is the issue of valuation of goods arises where the rates of duty are ad valorem, i.e., expressed as a percentage of the value of goods. For this purpose the assessable value of the goods has to be determined. There are three main ways for valuation in case the duty is ad valorem: (i) a tariff value that is fixed by the government in respect of certain goods; (ii) transaction value, and (iii) valuation based on the retail sale price printed on a package of goods.

The Central Government has power to fix tariff values in respect of goods under Section 3(2) of the Excise Act. In such a case, the assessee pays the ad valorem duty on the tariff value as fixed. In cases where either a tariff value has not been fixed by the Central government or the valuation is not based on the retail sale price, the valuation of goods is required to be carried out under Section 4 of the Excise Act. In such cases, valuation is based on the ‘transaction value’ of the goods. The concept of ‘transaction value’ was introduced in the Excise Act with effect from July 1, 2000, subject to the following conditions:

1. The price must be the sole consideration for the sale. In other words, the assessee must not receive any other sum either by way of money or by way of any other assistance for the manufacture of goods or any manufacturing assistance from the buyer.

2. The buyer of the goods must not be related person. The term related person has been defined in sub-section (3) (b) of Section 4 of the Excise Act.

3. Goods must be sold by the assessee for delivery at the time and place of removal.

The transaction value includes any amount that is paid or payable by the buyer to or on behalf of the assessee on account of the sale of goods. However, for determining the transaction value the duty of excise, sales tax and other taxes, actually paid or payable are not to be included. If any one of the above-mentioned three conditions is not satisfied then the value of the goods is determined in such manner as may be prescribed. For this purpose, the Central Government has framed the ‘Central Excise Valuation (Determination of Price of Excisable Goods) Rules, 2000’. These rules provide the manner for determination of value of goods which do not satisfy the above-mentioned conditions.

With effect from May 14, 1997 Section 4 A was inserted in the Excise Act. Under this provision, valuation of products may be made with reference to the retail sale price of the products. However, the conditions precedents for the application of the section are:
1. The excisable goods must be packaged goods on which there is a requirement to specify the retail sale price under the provisions of the Standards of Weights and Measures Act, 1976 or the rules framed there under or any other law for the time being in force;

2. The excisable goods are notified by the Central Government for purposes of the section; and

3. The goods must be chargeable to duty based on their value.

On satisfaction of these three conditions, the value for purposes of levy of excise duty shall be the retail sale price of such goods less such amount of abatement from such retail sale price as the Central government may notify. The abatement is given as a percentage of the retail sale price.

In the Cenvat system, the provision of Cenvat credit has been put in place since all manufactured goods are not used by end-users or consumers. The final products manufactured by some manufacturers may be the raw material/input for other manufacturers. Similarly capital goods purchased by a manufacturer may be utilised by him for setting up a plant, machinery or a factory. The inputs/capital goods so purchased by the manufacturer are duty paid. In order to overcome the cascading effect of tax, under the Cenvat Credit Scheme, a manufacturer or a service provider may take credit, inter-alia, of excise duty or additional duty of customs (levied under Section 3 (1) of the Customs Tariff Act, 1975) or service tax paid on the inputs or capital goods or inputs services and adjust such credit for making payment of tax on his final products or output services.

The law relating to valuation of excisable goods chargeable to ad valorem rate of duty under Section 4 of the Central Excises and Salt Act, 1944 has been the subject mater of a large number of disputes for a long time, beginning from the famous Voltas case where the dispute was as to what constituted ‘wholesale cash price’ and, when wholesale cash price was available, whether the department could have recourse to retail price as the basis for assessment. The Supreme Court coined concepts like Manufacturing cost plus the manufacturing profit, post-manufacturing cost and profit, which were not understood in the true spirit and were interpreted to the disadvantage of the revenue. In later cases which came up before the Supreme Court a decision about the interpretation of old Section 4 as well as new Section 4 (which came in force in October 1975) was rendered. The law on central excise valuation has gradually emerged through ruling of the Supreme Court in different cases.
e. Exemptions and Multiple Rates

The most significant cause of complexity is, of course, the existence of exemptions and multiple rates, and the irrational structure of the levies. These deficiencies are the most glaring in the case of the Cenvat and the Service Tax. The starting base for the Cenvat is narrow, and is being further eroded by a variety of area-specific, and conditional and unconditional exemptions. A few years ago the government attempted to rationalize the Cenvat rates by reducing their multiplicity. However, the government has not adhered to this policy and reintroduced concessionary provisions for several sectors/products.

In summary, since Cenvat relates to an artificial fragmentation of the value added space, it has led to several problems regarding definition, classification, and valuation.

2.3 Levy of Service Tax: Disputes

The present disjointed levy of service tax has also been equally complicated. Ever since the service tax was levied as a distinct and separate tax, it was subjected to several disputes. The key problem with the service tax is the basic approach of levying it on specified services, each of which generates an extensive amount of argumentation as to what is included in them. Ideally, the tax base should be defined to include all services, with a limited list of exclusions, that is, specifying only a negative list. The validity of service tax levy has been challenged in various courts of India from time to time. Some important decisions in this regard are given below.

The Gujarat High Court in the case of *Addition Advertising vs. Union of India (1998 (98) ELT 14)* has held that levy of tax on advertising service is not unconstitutional. It was held that this is not a tax on any profession, trade, calling or employment, but in respect of service rendered. If there is no service, there is no tax. It was further held that ‘the tax is not on advertisement’ but on the services rendered with reference to the advertisement and there is a clear distinction between the advertisement service and advertisement.

In another case of *M/s. Laghu Udyog Bharati vs. UOI (1999 (89) ELT 247)* the petitioners challenged the Government’s decision to shift the burden of duty liability to the service receivers in case of Goods Transport Operators and Clearing & Forwarding Agents. In this case, the Hon’ble Supreme Court upheld the contention of petitioners and held that the relevant provisions of Service Tax Rules were *ultra vires* the Finance Act, 1994. The Hon’ble Supreme Court while deciding the case, observed as follows :-

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“The service tax is levied by reason of services which are offered. The imposition is on the person rendering the service. Of course, it may be indirect tax, it may be possible that the same is passed on to the customer but as far as the levy and assessment is concerned, it is the person rendering the service who alone can be regarded as an assessee and not the customer. This is the only way in which the provision can be read harmoniously. The charge of tax is on the value of services and it is only the person who is providing service can be regarded as an assessee. The rules, therefore, cannot be so framed which do not carry out the purpose of the Chapter (Statute) and cannot be in conflict with the same.”

A number of trade bodies and individual service providers had challenged the levy of service tax by the Union Government under the Residuary Entry No.97, List I in Seventh Schedule of the Constitution. They contended that the service tax is nothing but a tax on professions, which is specifically listed, in the State list. Therefore, the Union Government is not empowered to levy service tax on professional services. Additionally, the levy has also been challenged on the grounds of hostile discrimination vis-à-vis other services and/or the service providers within the same category. The Institute of Architects and certain representative bodies of Chartered Accountants were the main bodies making these representations.

The Gujarat High Court in its judgement dated 27.12.2000 (in SCA No.469/1999 and 7220/1999) and the Mumbai High Court in the judgement dated 22.02.2001 (in the W/P no. 142/1999 and 1174/2000) have held that the tax on profession (which is in the State list) is a tax on the privilege of carrying on such profession. Therefore, such a tax is irrespective of the fact whether professional does or does not render professional service for remuneration. Whereas the service tax is a levy, which has to be paid each time a professional renders services for remuneration. Thus, professional tax and service tax are different in pith and substance. Further, the legislature is competent to identify and reasonably discriminate between various services and service providers for the purposes of taxation. Therefore, there is no ground to challenge the levy on the grounds of discrimination. The Madras High Court has also taken the same view in a plethora of petitions pending before them.

Considering the importance of early resolution of these disputes, the Directorate actively pursued such cases pending in Ahmedabad, Mumbai and Chennai High Courts that have upheld the constitutional validity of the service tax law provisions contained in the Chapter V of the Finance Act, 1994 as amended and the Rules framed there under.
Service tax on taxable services rendered in India are exempt, if payment for such services is received in convertible foreign exchange in India and the same is not repatriated outside India. The Cenvat Credit Rules allow a service provider to avail and utilize the credit of additional duty of customs/excise duty for payment of service tax. Credit is also provided on payment of service tax on input services for the discharge of output service tax liability.

2.4 Nature of Modern Services

The distinction between goods and services is increasing getting blurred with the advancements in information technology and digitization. Under Indian jurisprudence, goods have been defined to include intangibles, e.g., copyright, and software, bringing them within the purview of state taxation. But intangibles are often supplied under as part of a service contract. Software upgrades are considered as ‘goods’ but these can be supplied as part of a contract for software repair and maintenance services. The modern telecommunications give scope of providing many ‘value-added services’ (VAS) that may include supplies of ‘goods’ like wallpapers, ring tones, or weather reports for mobile phones. An on-line subscription to newspapers could be viewed as a service, but online purchase and download of a magazine or a book could constitute a purchase of goods. Leasing of equipment without transfer of possession and control to the lessee may be interpreted as a service but may be deemed as sale of goods.

The traditional distinctions between goods and services (and for other items such as land and property, entertainment, and luxuries) have become dated. In modern economies, goods and services are being bundled together and offered to the consumers as a composite bundle. Under the current division of taxation powers, neither the Centre nor the States can apply the tax to such bundles in a seamless manner. Each can tax only parts of the bundle, creating possibility of gaps and/or disputes.

2.5 Problems of State VAT

The complexities under the State VAT relate primarily to classification of goods to different tax rate schedules. Traditionally, the lower tax rates are applied to basic necessities. This is not the case under the State VAT. The lowest rate of 1 per cent applies to precious metals and jewellery and such other items made of them. The middle rate of 4 per cent applies to selected items of basic necessities and also a range of industrial inputs and IT products. In fact, basic necessities fall into three categories – exempted from tax, taxable at 4 per cent, and taxable at the standard rate of 12.5 per cent.
Another source of complexity under the State VAT is determining whether a particular transaction constitutes a sale of goods. This problem often arises when dealing with software products and intangibles like a right to distribute/exhibit movies or time slots for broadcasting advertisements.

Local or other state level taxes like octroi, entry tax, lease tax, workers contract tax, entertainment tax and luxury tax are not integrated into the State-VAT regime, which goes against the basic premise of VAT which is to have uniformity in the tax structure.

There is considerable heterogeneity across states because they have gone different schemes of schedular organization of goods.

2.6 Continuing Cascading

Tax cascading occurs under both the Centre and the State taxes. The most significant contributing factor to tax cascading is the partial nature of the taxes levied by them. Oil and gas production, and mining, agriculture, wholesale and retail trade, construction, and range of services remain outside the ambit of the Cenvat and the service tax levied by the Centre. The exempt sectors are not allowed to claim any credit for the Cenvat or the service tax paid on their inputs. Similarly, under the State-VAT, no credits are allowed for the inputs of the exempt sectors, which include the entire service sector, real property sector, agriculture, oil and gas production and mining. Another major contributing factor to tax cascading is the CST on inter-State sales, which is collected by the state of origin and for which no credit is allowed.

Poddar (2008) highlights that under the Canadian manufacturers’ sales tax, which was similar to the Cenvat, the non-creditable tax on business inputs and machinery and equipment accounted for approximately one-third of total revenues from the tax. The extent of cascading under the provincial retail sales taxes in Canada, which are similar to the State-VAT, is estimated to be 35-40 per cent of total revenue collections. He argues based on an earlier study by Kuo and Poddar (1998) that on *a priori* considerations, the expectation is that the magnitude of cascading under the Cenvat, service tax, and the State-VAT to be even higher, given the more restricted input credits and wider exemptions under these taxes. It is also clear that the service tax which is predominantly on business to business (B2B) services and remains highly cascading in nature.

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2.7 Continuation of Central Sales Tax

The continuation of CST is also a cause for cascading. Not allowing tax credit for inter-state trade seriously undermines the basic benefit of enforcing a vat system, namely the removal of the distortions in movement of goods across the states. CST creates unnecessary tax barriers in achieving an all-India integrated market. Further, the denial of input tax credit on inter-State sales and inter-State transfers would affect free flow of goods. Elimination of CST would be a prerequisite for implementing a proper goods and services tax.

2.8 Rationale for Extending Services for State Taxation

In order to resolve these problems, two changes need to be brought about simultaneously: extension of all services within the purview of State-VAT and extension of value added up to the retail level in the case of goods to be brought under the purview of the Cenvat. This is what the Kelkar Committee had called the ‘grand bargain’. These changes will have the effect of integrating for goods and services for purposes of taxation under the value added system.

We can cite at least four reasons why services should be extended for taxation along with goods for State-VAT. The first is a revenue reason. Given that services are fast growing sector (Table 2.1), this will ensure that states will share in the revenue buoyancy of the GDP via services. This is so because the share of consumption expenditure will progressively increase in favour of services. This will also make state revenue more stable since the services are the least volatile of the output sector in an economy. Table 2.1 gives a comparative picture of the relative growth performance of the different components of GDP.

The second reason is that expanding the taxation of services as part of the VAT system will make the sales tax fairer. The sales tax is intended to be a general tax on consumption where consumption of goods and services are often substitutes and should treated on par. It violates the principle of horizontal equity, for example, to tax the person who rents a videotape but not the person who watches a pay-per-view movie on cable TV.

Thirdly, taxing services at the same rate as goods would improve the allocation of economic resources. Differential rates or lower rates for services distort resource allocation by providing an incentive to purchase services rather than goods.
Table 2.1
Growth Rates of Agricultural and Allied Activities, Industry and Services Sectors
(1999-00 Base series: Constant Prices)

<table>
<thead>
<tr>
<th>Year</th>
<th>Agriculture and Allied Activities</th>
<th>Agriculture</th>
<th>Industry</th>
<th>Mining and Quarrying</th>
<th>Manufacturing</th>
<th>Electricity, Gas and Water Supply</th>
</tr>
</thead>
<tbody>
<tr>
<td>1950-60</td>
<td>2.71</td>
<td>2.93</td>
<td>5.99</td>
<td>4.07</td>
<td>6.12</td>
<td>10.32</td>
</tr>
<tr>
<td>1961-70</td>
<td>1.51</td>
<td>1.27</td>
<td>5.15</td>
<td>5.03</td>
<td>4.74</td>
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<td>1971-80</td>
<td>1.74</td>
<td>1.94</td>
<td>5.07</td>
<td>4.62</td>
<td>4.89</td>
<td>7.39</td>
</tr>
<tr>
<td>1981-90</td>
<td>2.97</td>
<td>3.09</td>
<td>6.41</td>
<td>7.39</td>
<td>5.95</td>
<td>8.76</td>
</tr>
<tr>
<td>1991-00</td>
<td>3.34</td>
<td>3.36</td>
<td>6.63</td>
<td>4.41</td>
<td>6.91</td>
<td>7.30</td>
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<td>2001-07</td>
<td>2.79</td>
<td>2.85</td>
<td>7.12</td>
<td>5.63</td>
<td>7.63</td>
<td>5.21</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Year</th>
<th>Service</th>
<th>Construction</th>
<th>Transport and Communication</th>
<th>Financing, Insurance, Real Estate &amp; Business services</th>
<th>Community, Social, and Personal Services</th>
<th>GDP at factor cost</th>
</tr>
</thead>
<tbody>
<tr>
<td>1950-60</td>
<td>4.34</td>
<td>5.87</td>
<td>5.29</td>
<td>3.05</td>
<td>3.51</td>
<td>3.66</td>
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<tr>
<td>1961-70</td>
<td>4.94</td>
<td>6.87</td>
<td>4.77</td>
<td>3.11</td>
<td>5.24</td>
<td>3.36</td>
</tr>
<tr>
<td>1971-80</td>
<td>4.36</td>
<td>3.06</td>
<td>5.40</td>
<td>4.44</td>
<td>3.68</td>
<td>3.41</td>
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<tr>
<td>1981-90</td>
<td>6.35</td>
<td>3.73</td>
<td>5.93</td>
<td>9.26</td>
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<tr>
<td>1991-00</td>
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<td>4.84</td>
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<td>7.95</td>
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<td>12.02</td>
<td>10.85</td>
<td>8.76</td>
<td>5.79</td>
<td>7.42</td>
</tr>
</tbody>
</table>

Source (Basic Data): National Income Accounts, CSO

Fourthly, treating servicers and goods on par will minimize if not altogether eliminate classification disputes as whether a supply is of that of a good or a services. It will reduce both the administration costs and compliance costs enormously. Since states in India are precluded from taxation of services except those specific services that may be listed in the State List, this has given rise to difficulties in taxation of goods supplied as part of a composite works contract involving a supply of both goods and services, and under leasing contracts, which involve a transfer of the right to use goods without any transfer
of their ownership. Although these specific problems have been addressed by amending the Constitution to bring such transactions within the ambit of the tax on the sale or purchase of goods, services by themselves remain outside the scope of state taxation powers.

2.9 Rationale for Extending Taxation of Goods up to Retail for the Centre

Similar reason can be cited as grounds for extending the taxation of goods up to retail for the Centre. First, it will eliminate the need to define ‘manufacturing’. Every supply from one registered dealer of a good or service will then become taxable up to the retail stage. This will also eliminate most of the valuation problems since in the valuation will be determined by the market and the incentive to underestimate values will also be minimal as tax credits are to be claimed at all stages. Secondly, this will permit a symmetrical treatment of goods and services. Thirdly, the centre will be compensated for sharing the taxation of services with the states. Fourthly, taxation of goods all the way up to the retail stage will create a paper record of all goods leaving state boundaries making settlement of inter-State disputes far easier in implementing a destination based principle of taxation.

2.10 Conclusions

Even after the introduction of the principle of taxation of value added in India, its application has remained piecemeal and fragmented. Several problems continue with each segment of the system of taxation of goods and services as summarized below.

1. In the case of Cenvat, the issues relating to definition of manufacturing and methodology of valuation remain causing difficulties in implementation of the tax.

2. The problem of multiple rates remains although the tax rate structure is simpler than what it used to be. This leads to various classification disputes.

3. In the case of services taxation, problems relate to distinguishing between a good and a service. The distinction between the two is often blurred.

4. Exclusion of services from the tax base of the states potentially erodes their tax buoyancy in a growing economy.

5. Cascading has not been fully eliminated as there is cross cascading between Statevat, Cenvat, and central services tax.
6. The Central sales tax continues to cause artificial inter-State border boundaries and violating the destination based principle of taxation of goods and services.

7. Many of these problems can be addressed by extending the scope of taxation of services for the states and the scope of taxation of goods up to the retail stage for the centre.

This is not to underplay the importance of the success already achieved in bringing about a value added taxation mechanism in highly distorted system of taxation in India that existed prior to these reforms. However, the logic of reforms would remain incomplete until the goods and services are integrated for purposes of taxation of the value added in the process of production and sale of goods and until a countrywide integrated market is not created. In the next Chapter, we consider the options available for India for a comprehensive Goods and Services tax, given its federal structure of governance.
3

Integrating Goods and Services for Taxation:
Options for a Comprehensive GST

3.1 Introduction

A comprehensive value added tax requires encompassing both goods and services in a common tax base extending through the country, unfettered by state boundaries. This will be consistent with the provision of Article 301 of the Constitution, which provides that subject to the other provisions of this Part [of the Constitution, see Annexure 2 for details], trade, commerce and intercourse throughout the territory of India shall be free. Such a country-wide integrated market will also be ‘efficient’ from an economic viewpoint with a view to enabling the realization of the full potential of opportunities of economic growth. In a federal country like India, this requires careful handling of inter-State trade of goods and services.

Such a tax has already being proposed and discussed in the Indian context and is being referred to as a Goods and Services Tax (GST). For India, in making a transition to GST from the present system of Cenvat-State VAT-Service Tax and other related taxes, one has to take into account the present assignment of powers of taxation to the central and State governments, changes required in these to bring about a comprehensive GST, relative revenue-impact on the Centre and the States in the short run and over time as well as issues of co-ordination and harmonization with a view to achieving an effective and comprehensive market in the country for purposes of taxation of all goods and services.

In making this transition, the paramount objective should be to ensure that the basic federal structure in terms of the relative revenue and fiscal autonomies of the Central and State governments are not disturbed. The issue therefore is to find a suitable form of GST such that the relative positions of the two tiers of governments are not disturbed. In this Chapter, we examine some of the available options to bring about reforms to enable GST to be adopted in India.

It may be noted that although more than 135 countries levy VAT/GST including many federal countries, almost all of them quite successfully, a distinction is now being made between the ‘old’ type of VAT and the more ‘modern’ GST. New Zealand and Australia are cited as examples of the modern type of VAT. In these cases, the tax bases are wide enough to include many public services and food items, and the tax rate is single and low.
3.2 Towards Integration of Goods and Services for Taxation: Options for India

The introduction of Cenvat for capturing value added up to manufacturing in place of the central excises and the replacement of the state sales taxes by the State-VAT, adopted by all the states now, constitutes a significant first step towards a comprehensive GST in India. Both these however cover only goods. The service tax has been separate but in the case of service tax also the principle of giving rebate on tax on services already paid has been introduced. Taken together, these changes have provided useful starting points for a GST. The main issues that need to be resolved now relate to:

a) The form of GST: Whether the country should move to a national GST, or a system of state GSTs, or a concurrent dual GST or a non-concurrent dual VAT.

b) Required Constitutional changes: Depending on the choice of the form of GST, what will be changes in the constitution required to enable the transition from the present system to the selected GST form?

c) Treatment of special goods like food, housing, land and property, financial services, and public services.

d) Treatment of inter-State movement of goods and services such as transportation and telecommunication. Except in the case of a National GST, there will be issues in relation to the treatment of inter-State flows of goods as well as services.

e) Depending on the selected form, a decision will have to be taken as to the taxes of the Centre and the States that should be merged in the GST.

f) The Central government has limited administrative infrastructure while the states have larger manpower dealing with the administration of the sales and other indirect taxes. The transition to GST will require careful planning as to needed administrative infrastructure and responsibilities of the centre and the states in providing such infrastructure.

g) In all cases, there would be a tangible revenue impact on the centre and the states and this will have implications for system of transfers from the centre to the states.

The main options for selecting a suitable form of GST may be listed as follows:

a. National GST,

b. System of State GSTs,
c. System of non-concurrent dual GST, and

d. System of Concurrent Dual GST.

It is important also to recognize that the vertical imbalance, that is relative revenue raising powers of the central and the state governments prior to transfers, may be affected depending on the way the goods and services tax (GST) is implemented in India.

3.3 National GST

Under this option, the two levels of government would combine their levies in the form of a single National GST. Such a GST will by definition ensure a country-wide common market. Since the rate structure will be common for all states, there will be harmonization by definition and there will be no problems about inter-State trade. Collection of tax can be done by the centre or the states or a suitable combination. The basic problem would be that it would take away the fiscal and revenue autonomy of the states who will have to be compensated by a suitable revenue sharing mechanism possibly based on the destination principle so that there is a one-to-one link between the share of a state in the consumption of goods and services, and its share in the GST revenues. Some variant of such a tax is followed in Australia, Austria, Argentina, Germany, and Mexico. The conventional wisdom on VAT/GST seems to suggest that the only good VAT is one levied by the central government. For example, McLure (1993, 58) noted that “…it is not appropriate to assign the VAT to subnational governments.”

In the case of central GST, all the State-VATs will be subsumed in this central levy in consumption of goods and services. This would be like the Australian model. But this will increase vertical imbalance tremendously. In Australia, the implementation of GST led to a substantial increase in the vertical imbalance because the states agreed to forego a number of taxes assigned to them in favor of a national GST.

A provision will have to be made for distribution of the centrally collected VAT. Although a similar arrangement has been implemented in Australia, it will have a significant impact on the nature fiscal federal relations. States will lose their autonomy to fix rates and collect their own revenues. It is doubtful that states will agree to such an arrangement. The scheme of redistribution would also be required to follow a principle different from the one normally used by the Finance Commissions so that states are adequately compensated for the revenues that they would have otherwise earned through the existing system of State-VAT or sales taxes.
3.4 System of State GSTs

Under this option, the GST would be levied by the States only. The Centre will continue to levy customs duties, and may levy some excise duties on selected goods like petroleum and petroleum products. There will be considerable revenue loss to the centre and while this may require a reduction in the volume of fiscal transfers, it would also mean a reduction in the capacity of the centre to undertake equalizing transfers to the economically weaker states. The USA with its retail sales tax that are with the states is an important example of this type of arrangement. This option raises various issues of harmonization and inter-State flows of goods and services.

The European Union VAT (EUVAT) may also be considered as an example of a system of State-VATs among participating member countries of an Economic Union/federation. The EUVAT is a value added tax encompassing all member states in the European Union Value Added Tax Area. It taxes the consumption of goods and services in the European Union Value Added Tax Area. The EUVAT is levied after determining where the supply and consumption occurs. This decides which member state will collect the VAT and what VAT rate will be charged.

Different rates of VAT apply in different EU member states. The minimum standard rate of VAT throughout the EU is 15 per cent, although reduced rates of VAT, as low as 0 per cent, are applied in various member states on various types of supply (for example, newspapers and certain magazines in Belgium). The maximum rate in the EU is 25 per cent.

VAT that is charged by a business and paid by its customers is known as “output VAT” (that is, VAT on its output supplies). VAT that is paid by a business to other businesses on the supplies that it receives is known as “input VAT” (that is, VAT on its input supplies). A business is generally able to recover input VAT to the extent that the input VAT is attributable to its taxable outputs. Input VAT is recovered by setting it against the output VAT for which the business is required to account to the government. If there is an excess, a repayment may be claimed.

The Sixth VAT Directive of the EU requires certain goods and services to be exempt from VAT (for example, postal services, medical care, lending, insurance, betting), and certain other goods and services to be exempt from VAT but subject to the ability of an EU member state to opt to charge VAT on those supplies (such as land and certain
financial services). Input VAT that is attributable to exempt supplies is not recoverable, although a business can increase its prices so the customer effectively bears the cost of VAT.

This option also changes the vertical balance equations drastically although in favor of the states. The centre will then largely lose power to undertake transfers for purposes of horizontal transfers. Even to provide centrally provided public goods, it may need to save some sumptuary excises for itself. Otherwise it may have to depend on reverse transfers. The problem of inter-State harmonization and inter-state transactions will remain. For the case of an exclusive State-VAT regime, Keen and Smith suggested the system of Viable Integrated VAT (VIVAT). In this case, for all intermediate purchases, that is, sales between dealers, a uniform tax rate regime is advocated for sales between dealers. This would be applied to transactions within a state as also across states. The system of compensating VAT (CVAT) is also known as the Versano proposal has also been suggested in this context. Mclure Jr.(2000) suggested a modified version of the CVAT. In CVAT, uniform definitions and laws for the tax base in all jurisdictions are needed. States are allowed however to have there own tax rates with the proviso that all inter-state transactions are zero-rated for state VAT. The Central government levies a compensating VAT for all inter-state transactions. The rate of compensating VAT is common across states. For inter-state imports, a system of deferred payment of State- VAT and credit for compensating VAT is then put in place. The Compensating VAT is an additional federal level tax to ensure the tax revenues that might otherwise be lost due to cross-border tax evasion are not so lost.

At the present juncture of the Indian economy, the central government is not likely to accept the option of a full fledged State-GST as the centre needs resources for addressing the high degree of horizontal imbalance in the system. If the vertical imbalance in the system is not to be drastically altered, the concurrent and dual VAT regime seems to be most relevant in the current fiscal conditions of India.

3.5 System of Non-concurrent Dual GST

One recent suggestion (Poddar, 2008) has been about a system of non-concurrent Dual GSTs. In this case, the proposal is to let the states levy GST on all goods and the centre levy the GST on all services. No special effort would be needed for levying a unified central tax on inter-state services. The centre would withdraw from the taxation of goods. Even the revenues collected from the taxation of services could be transferred back to
the States, partially or fully. This option will not however resolve the difficulties in delineating supplies of goods and services and cascading between goods and services may remain a problem unless arrangements are put in place for cross-administration rebates on input taxes paid. In this case, the centre will required to rebate input tax paid on goods and states will be required to rebate input tax on services.

### 3.6 Concurrent Dual GST

Under this model a concurrent or dual GST is levied by the Centre as well as the States. This seems the most practical route as it can be implemented while maintaining the current pre-and post-transfer profiles of vertical imbalance. It would require that states be enabled to tax services and the service tax rate should be the same as that for goods. Alongside, Central government should be enabled to tax value added in the case of goods up to the retail stage. These changes would lead to a comprehensive and unified system of taxation of goods and services. The major problem in this case will be handling of inter-State transactions.

In dual VAT, central and State-VAT rates are applied. States have autonomy to determine the State-VAT rates. The Central-VAT is included in the tax base of the State-VAT. States therefore have an incentive to collect the central component, if they are asked to collect it.

#### a. Scheme Proposed by the Empowered Committee

A Committee of State Finance Ministers under the Chairmanship of Dr. Ashim Dasgupta, Hon’ble Finance Minister of West Bengal referred to as the Empowered Committee (EC) of State Finance Ministers has been deliberating on the various aspects of a comprehensive goods and services tax in the Indian federal context. While many aspects of the GST are yet to be decided upon, the EC has favoured a concurrent GST with a central and state GST components. After a draft discussion paper, the EC has now put forward a ‘First Discussion Paper’ for wide ranging discussions. The views expressed by the EC may be summarised as below.

##### a1. Draft Discussion Paper

The main features of the proposed GST model are summarized below:

1) For Centre, the following taxes would be subsumed under the GST are: Central Excise duties (extended up to the retail level), Additional Excise duties, Additional
Duty of Customs or CVD, CST and Service Tax including all cesses and surcharges. Except for essential services such as primary public health and primary public education, all services should be comprehensively covered under the GST. The Additional Duty of Customs (known as CVD) which is essentially an excise imports would be subsumed under GST and would be made up of the same two components viz. the Central GST and the State GST.

2) The major State taxes to be subsumed under GST are: VAT or Sales Tax; Entertainment Tax, Luxury Tax, Octroi or Entry Tax and Taxes on Lotteries, Betting and Gambling, and Purchase Tax, and electricity duty, and any cesses and surcharges levied by the State governments.

3) The Centre shall levy one component (Central GST or CGST) and the states / Union Territories shall levy the other (State GST or SGST). Both CGST and SGST should be applicable, to all transactions of goods and services.

4) HSN classification for goods should be used both for Central GST and State GST.

5) A classification for services should be evolved by examining international practice, while keeping in view the particular characteristics of India’s services sector.

6) Separate accounts should be maintained for the central and the state GST. While input tax credit (ITC) should be permitted within each of the taxes, cross flow between Central and State GST should not be permitted.

7) Both CGST and SGST should ideally be at single rates. However, certain categories of goods may need to be taxed at a rate lower than the standard rate, both for CGST and SGST.

8) Exports should be fully zero-rated i.e. exports should be relieved of the burden of all embedded taxes and levies, both Central and states.

9) Demerit goods such as alcoholic beverages and tobacco should be brought under GST with ITC. However, Excise duties (without ITC) should be levied over and above the GST by both the centre and the states.

10) Since crude and petroleum products are non-renewable resources, a similar model, as recommended for alcoholic beverages and tobacco, could be adopted. An alternative would be to, keep crude, motor spirit, and high speed diesel out of the purview of the GST. This would reflect current practice in India that does not allow ITC of petrol and diesel to downstream users.
11) The annual turnover threshold should be uniform for the Centre and the states.

12) Every taxpayer, to be assigned a common taxpayer identification number and should be required to submit one periodical return (i.e. same document) with one copy to the Central GST authority and the other to the concerned State GST authority.

13) Inter-State sales should be governed by the *destination* principle.

14) For operationalizing this, banks are to be used as an intermediary. It would require that the seller in the exporting State collects GST from the purchasing dealer in the importing State and deposits it in the designated bank to the credit of the importing State/Centre. The seller also provides details of all transactions, including details of purchasing dealer to the bank. The bank uploads the information on the GST Portal, through which the information becomes available to both the central as well as State Authorities. The purchasing dealer claims ITC on the basis of a digitally signed challan sent by the seller's bank. The importing State/Centre grants ITC on the basis of the credit received by them from the bank in the exporting State.

15) Under the GST exemptions should be minimized. The dual GST structure at the Central and the State levels should have a common list of exemptions. Specific provisions to provide limited flexibility to the states within a set of prescribed criteria may be incorporated in order to accommodate exemption of goods of local importance, and

16) CST would be eliminated.

The Draft Discussion paper circulated earlier by the Empowered Committee had clearly recognized the issue of negative externalities. In particular, it recognized the issues of ‘demerit goods’ and ‘non-renewable’ resources. It recommended as follows:

(i) Demerit goods such as alcoholic beverages and tobacco should be brought under GST with ITC. However, Excise duties (without ITC) should be levied over and above the GST by both the centre and states.

(ii) Since crude and petroleum products are non-renewable resources, a similar model, as recommended for alcoholic beverages and tobacco, could be adopted. An alternative would be to, keep crude, motor spirit, and high speed diesel out of the purview of the GST. This would reflect current practice in India that does not allow ITC of petrol and diesel to downstream users.

Union and State taxes on petroleum and related products contribute in the range of 35-
40 percent of the revenue on average from central excise duty as also significant shares of states tax revenues. At present, neither the Union government nor the State governments allow ITC on major petroleum products. The Empowered Committee suggested two alternatives. In the first model, all petroleum products should be subjected to GST (with ITC). Over and above the GST, both the centre and the states can levy additional excise duty (without ITC) at different rates subject to a floor. Alternatively, out of the basket of petroleum products, Crude, Motor Spirit (including ATF) and HSD could be kept outside the GST. This will leave a significant source of cascading in the system.

These proposals imply that the overall efficiency in production and sales will go up and the compliance costs will go down. Much will depend on the level at which the overall GST rate is fixed and its components for the central and the state GSTs. The state component of the GST rate is likely at best to be revenue neutral with respect of all-state revenues and will have a differential revenue impact on the states, some of which may need to be compensated by the centre. It may be difficult to set up a mechanism where the gainer states would compensate the states losing out in relative terms.

**a2. First Discussion Paper**

The First Discussion Paper of the Empowered Committee carries forward the ideas of the Draft Discussion Paper but comes clearly in favor of an integrated GST (IGST) for dealing with inter-state trade in goods and services.

a. The GST will have two components: one levied by the Centre (CGST) and the other to be levied by the States (SGST). The basic features of law such as chargeability, definition of taxable event and taxable person, measure of levy including valuation provisions, basis of classification etc. should be uniform across these statutes as far as practicable.

b. The CGST and SGST would be applicable to all transactions of goods and services made for a consideration except for the exempted goods and services, goods which are outside the purview of GST and the transactions which are below the prescribed threshold limits.

c. The CGST and SGST are to be paid to the accounts of the Centre and the States separately. It would have to be ensured that account-heads for all services and goods would have indication whether it relates to Central GST or State GST (with identification of the State to whom the tax is to be credited). Taxes paid against the
CGST and SGST will get input tax credit (ITC) within the CGST and SGST chains respectively but cross utilization of ITC between CGST and SGST would not be allowed.

d. The administration of the CGST will be with the centre and that of SGST with the States.

e. A uniform State GST threshold across States is desirable. A threshold of gross annual turnover of Rs.10 lakh both for goods and services for all the States and Union Territories may be adopted with adequate compensation for the States (particularly, the States in North-Eastern Region and Special Category States) where lower threshold had prevailed in the VAT regime may be kept at Rs.1.5 crore and the threshold for Central GST for services may also be appropriately high. Even now there is a separate threshold of services (Rs. 10 lakh) and goods (Rs. 1.5 crore) in the Service Tax and CENVAT.

f. The following Central Taxes should be, to begin with, subsumed under the GST: (i) Central Excise Duty, (ii) Additional Excise Duties, (iii) Excise Duty levied under the Medicinal and Toiletries Preparation Act, (iv) Service Tax, (v) Additional Customs Duty, commonly known as Countervailing Duty (CVD), (vi) Special Additional Duty of Customs (SAD), (vii) Surcharges, and (viii) Cesses.

The following State taxes and levies should be, to begin with, subsumed under GST: (i) VAT / sales tax, (ii) entertainment tax (unless it is levied by the local bodies, (iii) luxury tax, (iv) taxes on lottery, betting and gambling, (v) State cesses and surcharges in so far as they relate to supply of goods and services, and (vi) entry tax not in lieu of Octroi.

Alcoholic beverages would be kept out of the purview of GST as part of demerit goods. Sales Tax/VAT can be continued to be levied on alcoholic beverages as per the existing practice. In case it has been made VAT able by some States, then this may be continued. Tobacco products would be subjected to GST with ITC. Centre may be allowed to levy excise duty on tobacco products over and above GST without ITC. As far as petroleum products are concerned, i.e. crude, motor spirit (including ATF) and HSD would be kept outside GST as is the prevailing practice in India. Sales Tax could continue to be levied by the States on these products with prevailing floor rate. Similarly, Centre could also continue its levies. On Natural Gas, whether it should be kept outside the GST, a final view has not been taken yet.

In this model, the Centre would levy Integrated Goods and Services Tax (IGST) which
would be CGST plus SGST on all inter-State transactions of taxable goods and services with appropriate provision for consignment or stock transfer of goods and services. The inter-State seller will pay IGST on value addition after adjusting available credit of IGST, CGST, and SGST on purchases. The exporting state will transfer to the Centre the credit of SGST used in payment of IGST. The importing dealer will claim credit of IGST while discharging his output tax liability in his own State. The Centre will transfer to the importing State the credit of IGST used in payment of SGST. The relevant information will also be submitted to the Central Agency which will act as a clearing house mechanism, verify the claims and inform the respective governments to transfer the funds.

a3. Task Force of the Thirteenth Finance Commission

The Thirteenth Finance Commission had set up a Task Force for designing a suitable form of GST. The main recommendations of the Task Force are summarised below:

a. The GST should be a dual levy imposed concurrently by the Centre and the States, but independently to promote cooperative federalism consisting of the Central Goods and Services Tax (CGST) and the State Goods and Services Tax (SGST), which should be levied on a common and identical base. The tax base should comprehensively extend over all goods and services upto the final consumer point.

b. There should be no classification between goods and services in law so as to ensure that there is no classification dispute.

c. The GST should be structured on the destination principle. As a result, the tax base will shift from production to consumption whereby imports will be liable to both CGST and SGST and exports should be relieved of the burden of goods and service tax by zero rating. Consequently, revenues will accrue to the State in which the consumption takes place or is deemed to take place.

d. The CGST and SGST should be credited to the accounts of the Centre and the States separately. Since the CGST and SGST are to be treated separately, taxes paid against the CGST should be allowed to be taken as input tax credit (ITC) for the CGST and could be utilized only against the payment of CGST. The same principle will be applicable for the SGST. Cross utilization of ITC between the CGST and the SGST should not be allowed.

e. Keeping in view the compliance cost and administrative feasibility, small dealers (including service providers) and manufacturers should be exempted from the purview of both CGST and SGST if their annual aggregate turnover (excluding
both CGST and SGST) of all goods and services does not exceed Rs.10 lakh. However, like in most other countries, those below the threshold limit may be allowed to register voluntarily to facilitate sales to other registered manufacturers/dealers, limit competitive distortions and avoid inequities. Further, the threshold exemption limit should be uniform for both CGST and SGST and across States. With a view to reducing administrative and compliance burden, small dealers with annual aggregate turnover of goods and services between Rs.10 lakh to Rs.40 lakh may be allowed to opt for a compounded levy of one per cent, each towards CGST and SGST. However, no input credit should be allowed against the compounded levy or purchases made from exempt dealers.

f. Certain high value goods comprising of: (i) gold, silver and platinum ornaments; (ii) precious stones; and (iii) bullions (hereafter referred to as “high value goods”) are prone to smuggling due to high tax incidence thereby generating negative externalities in terms of social and economic disorder. Dealers in such high value items may, subject to the threshold exemption but without the ceiling of Rs. 40 lakh, may be allowed to opt for the compounded levy of one per cent, each towards CGST and SGST.

g. The Centre and the States should draw up a common exemption list which should be restricted to the following:

- All public services of Government (Central, State and municipal/panchayati raj) including civil administration, health services and formal education services provided by government schools and colleges, defence, para-military, police, intelligence and government departments. However, public services should not include railways, post and telegraph, other commercial departments, public sector enterprises, banks and insurance, health and education services;
- Any service transactions between an employer and employee either as a service provider, recipient or vice versa;
- Any unprocessed food article which is covered under the public distribution system should be exempt regardless of the outlet through which it is sold;
- Education services provided by non-governmental schools and colleges; and
- Health services provided by non-governmental agencies.

h. The following central taxes should be subsumed in the CGST:
Central Excise Duty (including Additional Excise Duties);

Service Tax;

Additional Customs Duty (commonly referred to as ‘CVD’); and

Surcharges and all cesses

The following State level taxes, should be subsumed in the SGST:

VAT/Sales Tax (including central sales tax and purchase tax);

Entertainment tax (other than levied by local bodies);

Entry taxes not in lieu of Octroi;

Other Taxes and Duties (includes luxury tax, taxes on lottery, betting and gambling, and all cesses and surcharges by States);

These were also recommended by the EC. In addition, the Task Force recommends that the following other taxes levied by the Centre or the States, should be subsumed in the GST:

Stamp duty;

Taxes on Vehicles;

Taxes on Goods and Passengers; and

Taxes and duties on electricity.

i. The power sector is to be an integral part of the comprehensive GST. The tax regime for the power sector should be the same as in the case of any other normal good. The electricity duty levied by the States should be subsumed in the SGST.

f. The tax on vehicles and the tax on goods and passengers levied by the State Governments should also be subsumed in the GST. All transport equipments and all forms of services for transportation of goods and services by railways, air, road and sea must form an integral part of the comprehensive GST base recommended by the Task Force over which both the Central and State Governments would have concurrent jurisdiction. The tax regime for the transport equipments and transport services should be the same as in the case of any other normal goods.

j. The consumption of financial services should be comprehensively taxed under the GST framework on the basis of the full taxation method.
k. The real estate sector should be integrated into the GST framework by subsuming the stamp duty on immovable properties levied by the States to facilitate input credit and eliminate cascading effect. The GST should apply for all newly constructed property (both residential and commercial). If it is self-used by the person who constructed it, the GST should be applied on the cost of construction. If it is sold or transferred, the GST should be applied on the consideration received at first transfer or sale. In both cases, credit should be allowed in respect of input tax paid on raw materials used in construction. Also, rental charges received (excluding imputed rental values) in respect of leasing of immovable property used for both residential and commercial purposes should be charged to GST.

Sin Goods and Polluting Goods

The Task Force refers to the demerit goods as sin goods. The sin goods are listed as emission fuels, tobacco products and alcohol, which should be subject to a dual levy of GST and excise. No input credit should be allowed for this excise duty. However, industrial fuels should be subjected only to GST (both Central and State) with the benefit of input credit like any other intermediate good.

Any amount collected through these taxes on the SIN goods should not be subsumed either in the CGST or the SGST. Similarly any amount which is collected as tax/fee/charge/cess which is essentially in the nature of a user charge for supply of goods and services (including environmental goods and services) also should not be subsumed under the CGST or SGST. Further, both Centre and the States should take steps to consolidate all taxes (other than proposed GST) on the sin goods as a single levy termed as Central Excises and State Excises, respectively. All entry and Octroi duties levied by the third-tier of Government must be abolished.

Thus, the Task Force on GST set up by the 13th Finance Commission recognized the issue of negative externalities in a clearer way and collectively refers to these as sin goods and services and makes a distinction between sin goods and non-sin goods. The Task Force defines sin goods as goods whose consumption create negative externalities and for the purposes of their Report it, collectively or severally, refers to emission fuels, tobacco goods and alcohol. It observes that emission fuels generate negative externalities, whose consumption needs to be checked. It notes that generally, goods with negative externalities should be subjected to excise duties in respect of which input tax credit is not allowed.
Modified Bank Model: Inter-State Transactions of Goods and Services

Instead of IGST, the Task Force recommends adoption of a Modified Bank Model (the Bank Model was referred to in the EC Draft Discussion Paper) and suggests that all inter-State transactions in goods and services should be effectively zero rated by adopting the Modified Bank Model. The consignment sales and branch transfers across states should be subject to treatment in the same manner as if it was an inter-State transaction in the nature of sale between two independent dealers.

3.7 Constitutional Changes

Depending on the selected form of the GST, there will be a need to bring about constitutional changes so that both the centre and the states are ensured of their relative powers and the arrangements remain stable. If the Empowered Committee option of dual GST is adopted, centre will have to be given powers to tax the value added up to the retail stage in the case of goods instead of only up to manufacturing and the states will need to have power to tax all services. The service tax will need to be taken from Article 268 and the GST should be covered by Article 270. It would be best to place ‘taxation of goods and services’ in the concurrent list and delete all the individual taxes of the Union List and State List subsumed in it. Article 268 A will not be required and Article 270 should specifically make mention of the central GST.

In regard to the constitutional Amendments, there are several issues.

At present the Constitution of India demarcates taxing powers in a two-tier structure wherein levies on production and international imports are with the Union and post-production levies rest with the States. The tax bases for both the Centre and the States are different under the principle of separation of tax powers. Schedule VII divides this subject into three categories:

- Union List (Article 246 (1) of the Constitution specified that Parliament has exclusive powers to make laws with respect of any of the matters enumerated in List I in the Seventh Schedule to Constitution)
- State List (As per Article 246 (3) State Government has exclusive powers to make laws with respect to matters enumerated in List II)
- Concurrent List (both Parliament and State Government can pass legislation
The dual GST would require giving the Centre and the States identical indirect taxation powers. The incidence of tax will be restricted to consumption within the territory of the taxing jurisdiction. With concurrent powers, both the Centre and the States, one option is that the powers of the legislation of GST on supply of goods and services be assigned to the Centre and the States in the Concurrent List-III. However, this option has several problems. It changes the basic structure of the Constitution. The entry ‘GST on supply of goods and services’ in List-III would authorize the Centre and the States to frame Concurrent legislation on GST. This will mean that the centre will have over-arching powers. The States should have autonomy in exercise of their taxation powers.

The Constitution was designed to provide revenue autonomy to the state governments so that they can fulfill the responsibilities assigned to them as enumerated in the State List and Concurrent List of the Seventh Schedule to the Constitution. Revenue autonomy implies the power to change tax rates, define the tax base, define the exemption provisions, introduce rate categories where needed with respect to the areas assigned for taxation to the states. The Constitution has provided for separation of powers between the Union and the State governments so that within their assigned areas of jurisdictions, State legislatures and Parliament have full authority in terms of raising revenues and incurring expenditures to meet the responsibilities.

There is a clear link between revenue and expenditure autonomy both as per the constitutional design and principles of public economics. Expenditure autonomy is required so that State legislatures can recognize the preferences of the citizens under their jurisdiction regarding the nature and extent of regional or local public goods. The provision of these goods should be financed by taxation of the citizens under the same jurisdiction. Hence there is need for revenue autonomy. These powers are provided under the Constitution. The powers of the legislation of GST on supply of goods and services can be assigned to the Centre and the States in List-I and List-II respectively.

### 3.8 Determining the Overall Rate and Central and State Components

All important issue is to determine a suitable GST rate. At present goods are taxed at the core rate of Cenvat at 10 per cent and State-VAT of 12.5 per cent. This together would be very high although it would be less than 22.5 per cent as the 10 per cent rate applies to
value added only up to the manufacturing stage and the GST will have a larger base. The service tax rate has been at 12 per cent although it was reduced to 10 per cent in the context of the economic slowdown. The highest GST rates are in Sweden and Denmark at 25 per cent. At the lower end, Switzerland, Japan, Thailand and Singapore have GST/VAT rates at 5 per cent or marginally above. Appendix Table A5 and A6 give a summary of the international VAT/GST rates.

In relation to the rates in vogue in many countries, except the Scandinavian countries where the tax is levied at the standard rate of 25 per cent, a 20 per cent overall rate is too high. In New Zealand, GST was introduced at the rate of 10 per cent, with a base consisting of virtually all goods and services (with the exception of financial services). Singapore GST rate was 3 per cent at inception, which has now been raised to 7 per cent.

A large tax base enables a relatively lower tax rate to be revenue-neutral. The lower the revenue-neutral tax rate, the lower will be the demand for concessional rates or exemptions or zero-rating. A single rate GST comprehensively covering all goods and services at a single rate will be most conducive to tax compliance and rule out all classification disputes and other legal issues and minimize scope of evasion or avoidance.

There will be however issues related to selected goods and services like food, public services, etc. With a low single rate, much of support for basic necessities should be handled by government expenditure. Determining a suitable overall GST rate(s) and its CGST and SGST components is a critical component in planning the transition.

A related issue relates to decomposing the overall GST rate into its central and state components making sure that the relative pre-transfer revenue levels are not disturbed. The Kelkar Committee had suggested a division of the overall rate of 20 per cent into a 12:8 ratio in favor the centre. This may need to be reexamined with current levels of revenues under Cenvat and service taxes and the Statevat and other related taxes that may be subsumed in the GST.

Bagchi and Poddar (2007, Economic Times) have estimated of the size of the GST base in India and the GST rates that would be required to replace the current indirect tax revenues of the Centre and the States. They show that if the GST were to be levied on a comprehensive base, the combined Centre-State revenue neutral rate (RNR) need not be more than 12 per cent. This rate would apply to all goods and services, with the exception of motor fuels which would continue to attract a supplementary levy to maintain the
total revenue yield at their current levels. In the exercise by Bagchi and Poddar, for the RNR calculations, data for 2005-06 were used. The total excise/service tax/VAT/sales tax revenues of the Centre and the States in that year were Rs.1,34,000 crore and Rs.1,39,000 crore respectively. They estimate that the overall revenue neutral GST rate is 11.3 per cent with the RNR for the Centre at 5 per cent and that for the states at 6.3 per cent. Allowing for some leakages, the combined RNR could be in the range of 12 per cent.

In a recent study Kavita Rao (2008) estimates the revenue neutral GST rate using two methods, namely, a GDP based method and a consumption expenditure based method. Following the GDP –based method she estimates the revenue neutral GST rate to be about 14 with a 10 per cent rate of non-rebatable excises on passenger cars and multi-utility vehicles, petroleum products, and tobacco products. Following the consumption expenditure method she observes that the rate of GST required for revenue neutrality would be 20 per cent. With improved tax administration, the GST rate can be reduced further.

The Task Force of the Thirteenth Finance Commission has estimated with reference to a comprehensive tax base (as discussed in this chapter) a revenue neutral rate of 12 per cent, with 5 per cent for the centre, and 7 per cent for the states.

Table 3.1 indicates that overtime the relative share of the GST components for the Centre and the States have been changing marginally away from the Centre due to the erosion of buoyancy of Union excise duties.

The Task Force has recommended a single positive rate, each for CGST and SGST on all goods and services. In addition, there should be a zero rate applicable to all goods and services exported out of the country. The Task Force favours a single rate structure GST and some international experience with VAT in support. States have said that a single rate of State GST for all goods and services will be highly regressive in India with its large low income population. It is mainly the articles of common consumption which are in the lower rate bands of VAT. The single revenue-neutral rate will definitely be much higher than the rate now prevailing at the lower bands. To deal with problem, the Task Force suggests a moderate threshold exemption level for registration of dealers. Consequently, all small dealers would remain outside the purview of the GST. The Task Force Report argues that the tax incidence on products sold through such dealers would be relatively lower. Since the poorer section of the society tend to make their purchases from such
### Table 3.1

Revenue Importance of Central and States Taxes for Determining GST Rate Shares (Rs. crore)

<table>
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<td>45.5</td>
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<td>Share of States (%)</td>
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<td>57.2</td>
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Table - 3.1 (contd.)

Revenue Importance of Central and States Taxes for Determining GST Rate Shares

(Rs. crore)

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<td>d) Surcharge on Sales Tax</td>
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<td>e) Receipts of Turnover Tax</td>
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<td>State Excise</td>
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<td>Taxes on Goods and Passengers</td>
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<td>7270.3</td>
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<td>Other Taxes and Duties</td>
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<td>51301.0</td>
<td>65000.0</td>
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<td>38035.0</td>
<td>46035.0</td>
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<td>0.0</td>
<td>10595.0</td>
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<td>State taxes: Group 1#</td>
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<td>State taxes: Group 1+Group 2##</td>
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<td>Centre + State I</td>
<td>299948.0</td>
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<td>Share of Centre (%)</td>
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<tr>
<td>Share of States (%)</td>
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<td>52.6</td>
<td>51.2</td>
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<td>Centre + States II</td>
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<td>373775.2</td>
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<td>523011.5</td>
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<tr>
<td>Share of Centre (%)</td>
<td>42.0</td>
<td>43.9</td>
<td>44.9</td>
<td>44.7</td>
<td>41.2</td>
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<tr>
<td>Share of States (%)</td>
<td>58.0</td>
<td>56.1</td>
<td>55.1</td>
<td>55.3</td>
<td>58.8</td>
</tr>
</tbody>
</table>

Source: Reserve Bank of India: State Finances and Central Budget Documents (Receipts Budget)

* Figures relate to revised estimates
# Group 1: All sales taxes, state excise duties, motor vehicle tax, tax on goods and passengers, taxes and duties on electricity, entertainment tax, other taxes on goods and services
## Group 2: land revenue, stamps and registration fees, urban immovable property tax
small and unregistered dealers, the consumption of any commodity by the poor would bear a relatively lower incidence of tax than the consumption of the same commodity by the relatively richer section of the society.

The Task Force has used the fiscal year 2007-08 as the base year for calculation of the RNR. For the purposes of estimation of the GST base, the Task Force used several alternative approaches and estimated the GST base under these methods. The various estimates of the GST Base for 2007-08 are summarized in Table 3.2. Since the five estimates are different, the Task Force adopts their average of Rs. 3125325 crore, as the size of the comprehensive GST base for 2007-08 for the purposes of estimating the RNR. Since the tax base for both the CGST and the SGST are proposed to be identical, the Task Force uses the same tax base for calculating the RNR for both levies.

Table 3.2
Estimation of GST Base and the RNR

<table>
<thead>
<tr>
<th>Sl. No</th>
<th>Description</th>
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<tr>
<td>A</td>
<td>Subtraction- Indirect Method</td>
<td>3073037</td>
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<tr>
<td>B</td>
<td>Consumption</td>
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</tr>
<tr>
<td></td>
<td>i. Task Force Estimate</td>
<td>3743077</td>
</tr>
<tr>
<td></td>
<td>ii. Chadha Estimate</td>
<td>3077952</td>
</tr>
<tr>
<td>C</td>
<td>Shome Index Method</td>
<td>2782809</td>
</tr>
<tr>
<td>D</td>
<td>Revenue Method</td>
<td>2949748</td>
</tr>
<tr>
<td>E</td>
<td>Average of all estimated GST Base</td>
<td>3125325</td>
</tr>
<tr>
<td>F</td>
<td>Centre’s RNR (%)</td>
<td>5.05</td>
</tr>
<tr>
<td>G</td>
<td>State’s RNR (%)</td>
<td>6.02</td>
</tr>
</tbody>
</table>

The Task Force estimated the RNR for the CGST at 5.0 per cent. Similarly, the RNR in respect of the state level taxes which are proposed to be subsumed in the SGST is estimated to be 7.0 per cent. The combined RNR is estimated to be 12 per cent. The Task Force also recommended the abolition of all entry and Octroi taxes by state governments and other sub-national governments.
3.9 Other Considerations

a. Administration and Harmonization

Administration and compliance will require considerable harmonization. Such harmonization will have to cover aspects like tax laws, taxpayer registration system, taxpayer identification numbers, tax forms, tax reporting periods and procedures, invoice requirements, place of supply and other rules, and consumption and cross-border trade information system. The Empowered Committee has already proposed a common taxpayer identification system.

b. Treatment of Land and Property

Another issue relates to the treatment of land and real property transactions in the dual GST system. In terms of international practices as well as theory, GST will not be sufficiently comprehensive until land and property are brought into its ambit. The Service tax has already been extended to rentals of commercial property and construction services. Another item requiring attention would be land and real property transactions. If these are brought in the ambit of GST, as is done in recent international experience, it would help reduce the overall GST rate considerably. In the GST/VAT of Australia, New Zealand, Canada, Singapore, and South Africa, for example, housing and construction services are treated like any other commodity. When a real estate developer sells a home (first time sales), it is subject to GST/VAT on the selling price that includes the cost of land, building materials, and construction services. Commercial buildings and factory sales as well as rental charges for leasing of industrial and commercial buildings are also subject to GST. Only two exceptions are generally provided for, namely, resale of used homes and private dwellings, and rental of dwellings. However, short-term residential accommodation (in hotels, for example) is normally subject to VAT. The levy of GST should be considered as distinct from stamp duty and registration fees, which is a fee for registering and documenting titles to property.

The Task Force of the Thirteenth Finance Commission has recommended including of property, housing and rent also in the GST base.

c. Treatment of Food

Certain categories of goods often require special treatment. In the case of foodgrains and cereals and related items that are generally exempt in the case of CENVAT and taxed at the concessional rate of 4 per cent or exempted in the case of State-VAT. In the GST, if
these items are exempted or zero-rated the revenue neutral rate would increase considerably since the share of these items is nearly one-third in the aggregate consumption expenditure. It may be better to handle the issue of food security through the expenditure side of the government budgets. The Task Force of the Thirteenth Finance Commission has also recommended this.

d. **Non-profit Sector and Public Bodies**

Supplies made or services provided by governmental bodies and non-profit organizations have been exempted from VAT on the grounds that such bodies are not engaged in a business and their activities are not commercial in nature. This requires reconsideration. For one thing, the dividing line between public administration and industrial/commercial activities often is not clear enough. Services like postal and telecommunication services, radio and television, etc. may be provided by the private sector and/or the government.

In the EUVAT, activities of the public sector are categorized as non-taxable, taxable, or non-taxable, or exempt. There is a need to carefully determine the non-taxable and exempt categories and keep these lists quite narrow. In the case of New Zealand and Australia, the GST treats all activities of public sector and non-profit bodies as fully taxable with the exception of revenues from taxes, interest and dividends, and gifts and charitable donations. In these GST systems, any distinction between public administration and commercial/industrial activities of the state or non-profit organizations is not considered relevant. In fact, being part of the VAT chain, these bodies are eligible to claim a full credit for their input VAT.

e. **Financial Services**

Financial services are exempted from VAT in most countries mainly because the charge for the financial services provided by banks and insurance companies is generally implicit in the interest, dividends, or annuity payments. Explicit fees can however be charged. In some case, like China, financial services are taxable under their business tax, without the provision of input tax credits. In India, financial services where an explicit charge is made, are generally subject to the service tax. These should be part of GST.

f. **Inter-State and International Transactions**

One of the main issues that need to be resolved is in regards to inter-state supply/
consumption of services. Many inter-State services have no unique place of supply. Take for example the supply of group health insurance to a corporation with employees throughout India, or auditing or business consulting services provided to a corporation or conglomerate with business establishments in several States. The determination of place of supply of such services is going to be somewhat arbitrary. However, such services are almost entirely B2B supplies, the tax on which is fully creditable to the recipient. The arbitrariness in the rules would thus have no impact on the final tax collections of the Centre or the States. Fortunately, many inter-State services are provided mainly by the organized sector (e.g., telecom, and transportation services). It would be possible to formulate basic rules and guidelines for this purpose taking into account international practices in this regard.

Ideally, VAT should be levied on the basis of the destination principle. In practice, in order to distinguish between the tax treatment of supply and consumption, certain rules need to be defined. A sale of goods is taxable if the goods are made available in or delivered/shipped to that jurisdiction. Based on international experience, particularly in the European Union, some rules can adopted for implementing a dual GST. In defining the place of supply of services and intangible property, a distinction is often made between supplies made to businesses (B2B) and final consumers (B2C). B2B supplies are generally defined to be made where the recipient is located or established, regardless of where the services are performed or used. This is particularly useful for advisory or consulting services for which the place of performance is not important. These services become zero-rated, thereby avoiding tax cascading. In the case of B2C services, generally the rule is these are taxable in the jurisdiction where the supplier is located.

Special rules should be applied to the mobile services. For transportation services, the place of supply is defined by reference to the point of origin or destination. For telecommunication services, the supply is made in the jurisdiction if the points of origin and termination are in that jurisdiction, or if one of the points is in the jurisdiction and the supply is billed to an account in the jurisdiction. The European Union provides some useful guidelines for mobile services. In the case of passenger transport, services are taxed according to the distances covered in different jurisdictions. In the case of intra-EU transport of goods, taxation is at the place of departure. If the customer is identified for VAT purposes in another Member State and provides the supplier with this VAT identification number, the service will be taxed in the Member State where the customer is identified. In the case of ancillary services to an intra-EU transport of goods, such as
the loading and unloading services, these are taxable in the Member State where these services are physically carried out. If rendered to a customer who is identified for VAT purposes in another Member State and he provides the supplier with this VAT identification number of that other Member State, the service is instead taxed in the Member State where the customer is identified.

For short-term car rentals, the place of supply is where the car is first made available to the customer, regardless of the place of its subsequent use. For long-term leases, place of supply could depend on the place of use of the vehicle. Often, similar rules are adopted for leases and rentals of other goods also.

3.10 Integrating Environmental Considerations

Treatment of polluting inputs and output in the context of environmental management is of critical importance in the context of GST as these inputs and output create negative externalities. Environmental considerations were also specifically referred to the Thirteenth Finance Commission in their ToR relating to the ecology and environment. This has special relevance in the context of the proposed GST whatever may be the form in which it is implemented. Proponents of eco-taxes have argued for a ‘green shift’ in taxation of goods and services, which implies that the overall tax burden does not increase on the system so that inefficiency costs of excess taxation such as deadweight losses, compliance costs, and administrative costs do not increase.

Pollution has serious implications for economic growth and welfare because of its impact on health, resource depletion, and natural calamities linked to climate change. There are two major groups of policy instruments for achieving pollution reduction: regulatory and market based economic instruments. Regulatory instruments prescribe emission standards or effluent limits. These require considerable information and involve significant administrative costs for implementation and monitoring. Market based instruments include taxes, subsidies, and trading instruments. In comparison with the regulatory policies, market based instruments may be able to reduce the costs of achieving a given level of environmental protection through incentives.

The main forms of pollution are atmospheric pollution, land degradation and soil pollution, water pollution, and noise pollution. Many forms of pollution have adverse effect on the local and state population.

All environmental legislations in India come under Criminal Laws. In implementation
of the laws as well as in judicial decisions, the issue is on compliance or no compliance, and not on the extent of compliance. The penalties for non-compliance are unrelated to the compliance costs. On the other hand the economic compliance cost increases with the level of pollution prevention or abatement. This type of pollution control regime creates an opportunity for corruption and rent-seeking. The present standards and control regime – particularly the ones based on technology standards and input usage norms – provides no incentive for polluters to search for and adopt environmentally sound cost minimizing technologies/practices.

Environmental Tax Reforms (ETR) constitute indirect, self-monitoring, incentive-based changes in the tax structure to achieve environmental objectives. These have the potential to induce appropriate environmental decisions through instituting an incentive structure by raising the relative costs of polluting inputs and outputs.

In undertaking reforms of the taxation of goods and services one needs to ensure that the ecological tax reforms are an integral part of the overall tax reforms. It should be recognized that in a value added tax regime, input taxes are to be fully rebated. As such, taxation of polluting inputs will be ineffective as the tax paid on the inputs will be fully rebated, unless a non-rebatable cess is levied on the inputs. The more appropriate method would be to tax outputs and introduce ecological considerations by taxing at a higher rate, outputs that are either polluting or use highly polluting inputs. Eco-taxes should be designed in an integrated way for taxation at the central, state and local levels. These should complement each other and should not be at cross purposes. Global sources of pollution or pollution where state boundaries are generally crossed should be taxed at the national level, regional sources at the state level, and pollution with strong local characteristics should be taxed at the local level. There should be inter-State coordination so that as result of taxation of polluting inputs and outputs, industries do not attempt to relocate in other states where eco-taxes are less stringent.

The issue of environmental consideration also opens up the possibility of giving some revenue and fiscal flexibility to both tiers of governments. As is done in European Union and other countries, the environmental considerations within the framework of a comprehensive GST requires that on certain outputs non-rebatable special duties be levied. This may be the only ground for levy of such special duties. Some of the items that may be covered under this provision are petroleum and related products, products involving extensive use of coal, plastics, lead, metals, alcoholic beverages the production of which involves pollution. Most of these items are the ones that have relatively inelastic demand.
As such, these can also serve as an instrument providing flexibility to the states to take into account local conditions in determining the relevant rates of special duties. These can also help the states in at least partially absorbing the revenue impact of moving to GST.

Special provisions have to be made in the case of the Special Economic Zones and Export Oriented Units who are given inputs including polluting inputs on a zero-rated basis. While their products may be exported or treated as imports if sold in the domestic economy, much of the pollution that they generate is affecting the geographical area in which they are located. Polluting inputs in their case should not be zero-rated. They should also be subject to all other applicable regulatory measures for pollution control.

Both the Empowered Committee and the Task Force have considered the issue under ‘demerit goods’ or ‘sin goods’. The Empowered Committee has made reference to ‘demerit goods’ and the Task Force setup by the Thirteenth Finance Commission has referred to these as ‘sin goods’. These concepts also allow for integrating environmental considerations into the GST regime as both of these relate to ‘negative externalities’ and good and services whose use need to be discouraged.

In its Draft Discussion paper, the Empowered Committee has discussed about the demerit goods including petroleum products (which, as already discussed, above are one of the main polluting goods in India). The Empowered Committee has argued in favour of keeping the demerit goods including petroleum products, tobacco, and alcohol out of the GST purview. These goods in turn will be subjected to separate non-debatable excise duties. In the Draft Discussion paper circulated by the Empowered Committee the following was recommended.

“….Demerit goods such as alcoholic beverages and tobacco should be brought under GST with ITC. However, Excise duties (without ITC) should be levied over and above the GST by both the centre and states.

Since crude and petroleum products are non-renewable resources, a similar model, as recommended for alcoholic beverages and tobacco, could be adopted. An alternative would be to, keep crude, motor spirit, and high speed diesel out of the purview of the GST. This would reflect current practice in India that does not allow ITC of petrol and diesel to downstream users.”

The Task Force set-up for the 13th Finance Commission clubbed the petroleum products,
tobacco and alcohol under the category ‘sin goods’. The Task Force recognized the issue of negative externalities in a clearer way and collectively referred to these as sin goods and services and makes a distinction between sin goods and non- sin goods. The Task Force defines sin goods as goods whose consumption create negative externalities and for the purposes of their Report these, collectively or severally, refer to emission fuels, tobacco goods and alcohol. The Task Force notes that generally, goods with negative externalities should be subjected to excise duties in respect of which input tax credit is not to be allowed.

It is suggested here that in the case of polluting goods and other natural resources, taxation should be considered as a potent instrument which should be used to curb both production and consumption. Accordingly, the Centre and the State governments should be allowed to levy non-rebatable excise and/or cesses on all polluting goods and natural resources (coal, petroleum, fertilizers, pesticides, textiles, plastics, leather, electricity) being mined out from their regions (coal, metals) and all potential health hazards for their citizens (alcohol, tobacco) at rates considered appropriate by them and Constitutional Amendments for introducing GST should leave adequate fiscal space for the levy of such excises/cesses.

3.11 Conclusions

In this Chapter, we have discussed various options available for India in selecting a suitable form of GST with the overall objective of achieving a comprehensive and integrated domestic market while maintaining the basic feature of our federal structure including the present level of vertical imbalance before and after transfers at least in broad terms. The following are some of the specific suggestions:

1. India should opt for a dual and concurrent system of GST.
2. The aggregate GST base should be large enough to permit a low single GST rate.
3. The rates for the central and state components should be determined taking into account not only the present relativities but likely growth of revenues of the taxes to be subsumed in the GST rate.
4. Petroleum and petroleum products, alcoholic beverages, and polluting inputs or outputs intensively using polluting inputs may be subjected to special non-rebatable levies (in the form of excise and cesses) both by the Central and
State governments. This should apply to all polluting goods and services also.

5. Exports should be zero-rated and inter-State flow of goods and services should be handled on the destination principle with limited exception of localized environmental damage where a special levy can be imposed by the producing state.

6. Exemptions should be minimized if not altogether avoided including foods and related items. All income or consumption support policies should be implemented through direct subsidy or explicit government expenditure rather than through tax expenditure implicit in tax exemptions.

7. The efficiency gains of a simple single rate system would be such that the extra revenue earned by both the tiers of government that India will be ushered into a modern productive economy with high growth rate.
Concluding Observations

4.1 Introduction

The Commission on Centre-State Relations has been asked as part of its Terms of Reference (ToR) to examine ‘the need and relevance of separate taxes on the production and on the sales of goods and services subsequent to the introduction of VAT regime’. In a federal economy like India, there are three issues that require examination in the context of this term of reference:

1. Whether there is any need or relevance for separation of production from sales in the case of goods.
2. Whether there is need or relevance for separation of goods from services in the context of taxation in a VAT system.
3. Whether there is need or relevance for separation of jurisdictions of the Central and the State governments in capturing the value added in the production and sale of goods as well as services.

This study has looked at the shortcomings of the existing system of taxation of goods and services in India, the rationale for further reforms leading to an integrated treatment of goods and services in a comprehensive all-India market, and a suitable form of a GST that can maintain the relative share of revenues of the central and State governments before and after transfers from the centre to the states so that the existing profile of vertical balance is not disturbed.

4.2 Taxation of Goods and Services in India: Existing Arrangements

The existing system of taxation of goods and services in India, even after considerable reforms, has many deficiencies although a sound beginning has been made in bringing about the principle of VAT of goods and services. At present, the system of taxation of goods and services consists of three disjointed parts: Cenvat (taxation of goods up to manufacturing by the central government), State-VAT (taxation of goods up to the retail level by the state governments), and taxation of services by the central government.
The taxation space up to the value added in the production of goods (up to manufacturing) is common between the Centre and the States. Different states can have their own variations in terms of rates and classification of goods. In the State-VAT system, an attempt has been made to arrive at a broad convergence of rates, but states have gone for their own classification schemes and there are many differences in the classification schemes. In addition to the State-VAT, the levy of a CST continues on inter-State sales.

While the system of taxation is thus characterized by fragmentation and overlaps in the case of goods, the taxation of services remains separated and disjointed from that of goods. With different tiers of government involved in taxation of value added in the case of goods, there is considerable cascading that result, which causes several inefficiencies and distortions. In particular, it favours imports, which are treated as final goods and bear the burden of taxation only once, against domestic production, which may be taxed several times; it increases the cash balance requirement of the producers/dealers; it makes tracing the overall tax burden of a good or a service difficult; and, it encourages tax evasion and compliance costs. In addition, in every type of tax, there are a large number of cesses and surcharges. Such a system does not meet the first principles of a good tax system and more reforms are needed.

The main problems of the existing system of taxation of goods and services are summarized below.

1. In the case of Cenvat, the issues relating to definition of manufacturing and methodology of valuation remain causing difficulties in implementation of the tax.
2. The problem of multiple rates remains although the tax rate structure is simpler than what it used to be. This leads to various classification disputes.
3. In the case of services taxation, problems relate to distinguishing between a good and a service. The distinction between the two is often blurred.
4. Exclusion of services from the tax base of the states potentially erodes their tax-buoyancy in a growing economy.
5. Cascading has not been fully eliminated as there is cross cascading between Statevat, Cenvat, and central services tax.
6. The CST continues to cause artificial inter-State border boundaries and violating the destination based principle of taxation of goods and services.

Many of these problems can be addressed by extending the scope of taxation of services for the states and the scope of taxation of goods up to the retail stage for the centre.

4.3 Changing Structure of the Indian Economy

It has been noted in this study that the structure of the Indian economy has been persistently changing in favour of services. The share of the agricultural sector has come down over the years, the share of manufacturing has increased to a limited extent, but the share of the services sector has been increasing steadily. The share of agriculture has come down from more than 55 per cent in 1950-51 to about 18.5 per cent by 2006-07. The share of industry, which was only about 11 per cent of GDP in 1950-51 now accounts for nearly 20 per cent. The share of services has increased to more than 60 per cent of GDP at factor cost by 2006-07. The service sectors show not only the relatively higher growth rates but also much less volatility in the growth rates.

4.4 Rationale for Similar Treatment of Goods and Services

The traditional distinction between goods and services (and for other items such as land and property, entertainment, and luxuries) has become dated. In modern economies, goods and services are being bundled together and offered to the consumers as a composite bundle. Under the current division of taxation powers, neither the Centre nor the States can apply the tax to such bundles in a seamless manner. Each can tax only parts of the bundle, creating possibility of gaps and/or disputes.

The distinction between goods and services is increasing getting blurred with the advancements in information technology and digitization. For example, under Indian jurisprudence, goods have been defined to include intangibles, e.g., copyright, and software, bringing them within the purview of state taxation. But intangibles are often supplied as part of a service contract. Software upgrades are considered as ‘goods’ but these can be supplied as part of a contract for software repair and maintenance services. The modern telecommunications give scope of providing many VAS that may include supplies of ‘goods’ An on-line subscription to newspapers could be viewed as a service, but online purchase and download of a magazine or a book could constitute a purchase of goods. Leasing of equipment without transfer of possession and control to the lessee is a service but may be deemed as sale of goods.
In order to resolve these problems, two changes need to be brought about simultaneously: extension of all services within the purview of State-VAT and extension of value added up to the retail level in the case of goods to be brought under the purview of the Cenvat. This is what the Kelkar Committee had called the ‘grand bargain’. These changes will have the effect of integrating goods and services for purposes of taxation under the value added system.

### 4.5 Rationale for Extending Services to States for Taxation

There are good reasons why services should be extended for taxation along with goods for State-VAT. The first is a revenue reason. Given that services are growing relatively faster than other sectors, extension of services for taxation by the states will ensure that the states share in the revenue buoyancy with respect to the GDP. This will also make state revenue more stable since the services are the least volatile of the output sector in an economy.

The second reason is that expanding the taxation of services as part of the VAT system will make the sales tax fairer. The sales tax is intended to be a general tax on consumption where consumption of goods and services are often substitutes and should treated on par. Thirdly, taxing services at the same rate as goods would improve the allocation of economic resources. Lower rates for services distort resource allocation by providing an incentive to purchase services rather than goods.

Fourthly, treating services and goods on par will minimize if not altogether eliminate classification disputes as to whether a supply is of that of a good or a services. It will reduce both the administration costs and compliance costs enormously. Since states in India are precluded from taxation of services except those specific services that may be listed in the State List, this has given rise to difficulties in the taxation of goods supplied as part of a composite works contract involving a supply of both goods and services, and under leasing contracts, which involve a transfer of the right to use goods without any transfer of their ownership.

### 4.6 Rationale for Extending Taxation of Goods up to Retail for the Centre

Similar reasons can be cited as grounds for extending the taxation of goods up to retail for the centre. First, it will eliminate the need to define ‘manufacturing’. Every supply from one registered dealer of a good or service will then become taxable up to the retail stage. This will also eliminate most of the valuation problems since valuation will be determined
by the market and the incentive to underestimate values will also be minimal as tax credits are to be claimed at all stages. Secondly, this will permit a symmetrical treatment of goods and services. Thirdly, the centre will be compensated for sharing the taxation of services with the states. Fourthly, taxation of goods all the way up to the retail stage will create a paper record of all goods leaving state boundaries making settlement of inter-State disputes far easier in implementing a destination based principle of taxation.

4.7 Towards a Comprehensive GST

Although various options may be considered in selecting a suitable form of GST for India, the option of a dual concurrent GST seems most practicable at the present juncture. Under this model a concurrent or dual GST is levied by the Centre as well as the States. This can be implemented while maintaining the current pre-and post-transfer profiles of vertical imbalance. It would require that states be enabled to tax services and the service tax rate should be the same as that for goods. Alongside, Central government should be enabled to tax value added in the case of goods up to the retail stage. These changes would lead to a comprehensive and unified system of taxation of goods and services.

The Empowered Committee of the State Finance Ministers has also recommended the concurrent dual GST. The main features of the proposed GST model are summarized below:

1) For Centre, the following taxes would be subsumed under the GST: Central Excise duties (extended up to the retail level), Additional Excise duties, Additional Duty of Customs or CVD, CST and Service Tax including all cesses and surcharges. Except for essential services such as primary public health and primary public education, all services should be comprehensively covered under the GST. The Additional Duty of Customs (known as CVD) which is essentially an excise on imports would be subsumed under GST and would be made up of the same two components viz. the Central GST and the State GST.

2) The major State taxes to be subsumed under GST are: VAT or Sales Tax; Entertainment Tax; Luxury Tax; Octroi or Entry Tax and Taxes on Lotteries, Betting and Gambling, and Purchase Tax, and electricity duty, and any cesses and surcharges levied by the State governments.
3) The Centre shall levy one component (Central GST or CGST) and the states / Union Territories shall levy the other (State GST or SGST). Both CGST and SGST should be applicable to all transactions of goods and services.

4) Separate accounts should be maintained for the central and the state GST. While input tax credit (ITC) should be permitted within each of the taxes, cross flow between Central and State GST should not be permitted.

5) Both CGST and SGST should ideally be at single rates. However, certain categories of goods may need to be taxed at a rate lower than the standard- rate, both for CGST and SGST.

6) Exports should be zero-rated i.e. exports should be relieved of the burden of all embedded taxes and levies, both Central and states.

7) Demerit goods such as alcoholic beverages and tobacco should be brought under GST with ITC. However, Excise duties (without ITC) should be levied over and above the GST by both the centre and states.

8) Since crude and petroleum products are non-renewable resources, a similar model, as recommended for alcoholic beverages and tobacco, could be adopted.

9) Inter-State sales should be governed by the destination principle.

10) Under the GST exemptions should be minimized. The dual GST structure at the Central and the State levels should have a common list of exemptions. Specific provisions to provide limited flexibility to the states within a set of prescribed criteria may be incorporated in order to accommodate exemption of goods of local importance; and

11) CST would be eliminated.

Union and State taxes on petroleum and related products contribute more than 40 per cent of the revenue from central excise duty as also significant shares of states tax revenues. At present, neither the Union government nor the State governments allow ITC on major petroleum products. The Empowered Committee has suggested two alternatives. In the first model, all petroleum products should be subjected to GST (with ITC). Over and above the GST, both the centre and the states can levy additional excise duty (without ITC) at different rates subject to a floor.

The Empowered Committee has since come out with the First Discussion Paper on GST.
It has suggested that petroleum products and alcoholic beverages should be left out of GST and central excise and state sales tax on these should continue. For tobacco, it has recommended levy of central excise alongwith CGST and SGST.

The Task Force set up by the Thirteenth Finance Commission has recommended a more comprehensive tax base for GST, which enables a reduction of the revenue neutral rate.

4.9 Need for Ensuring Revenue Neutrality in Transition

In order to main the relative profile of vertical balance in the share of revenues for the centre and states, a suitable GST rate needs to be determined and divided between a central GST rate and a state GST rate. The larger is the tax base, the lower can be the overall GST rate. Apart from some Scandinavian countries where the GST rate may be as high as 25 per cent, most other countries have settled for a comprehensive base and low rate with minimum exemptions. A single rate GST comprehensively covering all goods and services will be most conducive to tax compliance and rule out all classification disputes and other legal issues and minimize scope of evasion or avoidance.

The Kelkar Committee had suggested an overall rate of 20 per cent divided into a 12:8 ratio in favor the centre. This may need to be reexamined with current levels of revenues under Cenvat and service taxes and the Statevat and other related taxes that may be subsumed in the GST. Bagchi and Poddar (2007) an overall revenue neutral GST rate of 11.3 per cent with the central GST rate at 5 per cent and that for the states at 6.3 per cent. Allowing for some leakages, they suggest that the overall rate can be 12 per cent.

In a recent study Kavita Rao (2008) has estimated the revenue neutral GST rate using two methods, namely, a GDP based method and a consumption expenditure based method. Following the GDP-based method, she estimates the revenue neutral GST rate to be about 14 with a 10 per cent rate of non-rebatable excises on passenger cars and multi-utility vehicles, petroleum products, and tobacco products. Following the consumption expenditure method, she observes that the rate of GST required for revenue neutrality would be 20 per cent. With improved tax administration, the GST rate can be reduced further.

The Task Force of the Thirteenth Finance Commission has estimated the RNR at 12 per cent, 5 per cent for centre and 7 per cent for the states.
4.10 Need for Integrating Environmental Considerations

Another contextual issue, also specifically refereed to the Thirteenth finance Commission relates to ecology and environment. This has special relevance in the context of the proposed GST whatever may be the form in which it is implemented. It should be recognized that in a value added tax regime, input taxes are to be fully rebated. As such, taxation of polluting inputs will be ineffective as the tax paid on the inputs will be fully rebated, unless a non-rebatable cess is levied on the inputs.

As is done in European Union and other countries, the environmental considerations within the framework of a comprehensive GST requires that on certain outputs non-rebatable special duties be levied. Some of the items that may be covered under this provision are petroleum and related products, motor vehicles, products involving extensive use of coal, plastics, lead, metals, alcoholic beverages the production of which involves pollution. Most of these items are the ones that have relatively inelastic demand. As such, these can also serve as an instrument providing flexibility the states to take into account local conditions in determining the relevant rates of special duties. These can also help the states in at least partially absorbing the revenue impact of moving to GST.

Both the Empowered Committee and the Task Force bring into consideration the issue of negative externalities through the concept of ‘demerit goods’ and ‘sin goods’.

The Task Force recommended that environment polluting taxes should all be clubbed into a central excise and state excise, which should be non-rebatable.

Environmental taxes or eco-taxes constitute and indirect, self-monitoring, incentive-based instrument for pollution control. These have the potential to induce appropriate environmental decisions through instituting an incentive structure by raising the relative costs of polluting inputs and outputs. Also called ‘green taxes’, these are not necessarily meant as a revenue-augmenting device. Instead, the idea is to change the structure of taxation rather than putting additional burden on the tax payers. Environmental taxes may yield benefits over and above a cleaner environment. In particular, governments can use the revenues from pollution taxes to decrease other distortionary taxes, thereby providing a ‘double dividend’. 
4.11 Conclusions

Thus, for the overall objective of achieving a comprehensive and integrated domestic market encompassing all goods and services while maintaining the basic feature of our federal structure including the present level of vertical imbalance before and after transfers at least in broad terms, the following are some of the specific suggestions:

1. India should opt for a dual and concurrent system of GST.
2. The aggregate GST base should be large enough to permit a low single GST rate.
3. The rates for the central and state components should be determined taking into account not only the present relativities but likely growth of revenues of the taxes to be subsumed in the GST rate.
4. Petroleum and petroleum products, alcoholic beverages, and polluting inputs or outputs intensively using polluting inputs may be subjected to special non-rebatable levies (excise and cesses) both by the central and State governments.
5. Exports should be zero-rated and inter-State flow of goods and services should be handled on the destination principle with limited exception of localized environmental damage where a special levy can be imposed by the producing state.
6. Exemptions should be minimized if not altogether avoided including foods and related items. All income or consumption support policies should be implemented through direct subsidy or explicit government expenditure rather than through tax expenditure implicit in tax exemptions.
7. The Constitutional Amendment to bring about GST, should ensure that revenue autonomy of the states is not adversely affected.
8. The efficiency gains of a simple single rate system would be such that, with the extra revenue earned by both the tiers of government, India will be ushered into a modern productive economy with a sustained high growth rate for many years to come.
References


Annexure A1

Article 268. Taxes levied by the Union but collected and appropriated by the States

(1) Such stamp duties and such duties of excise on medicinal and toilet preparations as are mentioned in the Union List shall be levied by the Government of India but shall be collected—

(a) in the case where such duties are leviable within any [Union territory], by the Government of India, and

(b) in other cases, by the States within which such duties are respectively leviable.

(2) The proceeds in any financial year of any such duty leviable within any State shall not form part of the Consolidated Fund of India, but shall be assigned to that State.

Article 269. Taxes levied and collected by the Union but assigned to the States

(1) Taxes on the sales or purchase of goods and taxes on the consignment of goods shall be levied and collected by the Government of India but shall be assigned and shall be deemed to have been assigned to the States on or after the 1st day of April, 1996 in the matter provided in clause (2).

Explanation—For the purposes of this clause

(a) The expression “taxes on the sale or purchase of goods” shall mean taxes on sale or purchase of goods other than newspapers, where such sale or purchase takes place in the course of inter-State trade or commerce;

(b) The expression “taxes on the consignment of goods” shall mean taxes on the consignment of goods (whether the consignment is to the person making it or to any other person), where such consignment takes place in the course of inter-State trade or commerce.

(2) The net proceeds in any financial year of any such tax, except in so far as those proceeds represent proceeds attributable to Union territories, shall not form part of the Consolidated Fund of India, but shall be assigned to the States within which that tax is leviable in that year, and shall be distributed among those States in accordance with such principles of distribution as may be formulated by Parliament by law.
(3) Parliament may by law formulate principles for determining when a sale or purchase of, or consignment of, goods takes place in the course of inter-State or commerce.
Annexure 2: Article 301-307 of the Constitution

Article 301 Freedom of trade, commerce and intercourse: Subject to the other provisions of this Part, trade, commerce and intercourse throughout the territory of India shall be free.

Article 302 Power of Parliament to impose restrictions on trade, commerce and intercourse: Parliament may by law impose such restrictions on the freedom of trade, commerce or intercourse between one State and another or within any part of the territory of India as may be required in the public interest.

Article 303 Restrictions on the legislative powers of the Union and of the States with regard to trade and commerce: (1) Notwithstanding anything in Article 302, neither Parliament nor the Legislature of a State shall have power to make any law giving, or authorising the giving of, any preference to one State over another, or making, or authorising the making of, any discrimination between one State and another, by virtue of any entry relating to trade and commerce in any of the Lists in the Seventh Schedule.

(2) Nothing in clause (1) shall prevent Parliament from making any law giving, or authorising the giving of, any preference or making, or authorising the making of, any discrimination if it is declared by such law that it is necessary to do so for the purpose of dealing with a situation arising from scarcity of goods in any part of the territory of India.

Article 304 Restriction on trade, commerce and intercourse among States: Notwithstanding anything in Article 301, the Legislature of a State may by law -

(a) impose on goods imported from other States or the Union territories any tax to which similar goods manufactured or produced in that State are subject, so, however, as not to discriminate between goods so imported and goods so manufactured or produced; and

(b) impose such reasonable restrictions on the freedom of trade, commerce or intercourse with or within that State as may be required in the public interest:

Provided that no Bill or amendment for the purposes of clause (b) shall be introduced or moved in the Legislature of a State without the previous sanction of the President.
Article 305 Saving of existing laws and laws providing for State monopolies: Nothing in Articles 301 and 303 shall affect the provisions of any existing law except in so far as the President may by order otherwise direct; and nothing in article 301 shall affect the operation of any law made before the commencement of the Constitution (Fourth Amendment) Act, 1955, in so far as it relates to, or prevent Parliament or the Legislature of a State from making any law relating to, any such matter as is referred to in sub-clause (ii) of clause (6) of article 19.

Article 306 Power of certain States in Part B of the First Schedule to impose restrictions on trade and commerce:

Article 307 Appointment of authority for carrying out the purposes of articles 301 to 304: Parliament may by law appoint such authority as it considers appropriate for carrying out the purposes of Articles 301, 302, 303 and 304, and confer on the authority so appointed such powers and such duties as it thinks necessary.
## Appendix Table A1
The Changing Composition of Agricultural and Allied Activities and Industry Sectors (Constant Prices)

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Source (Basic Data): Central Statistical Organization; New Series (Base : 1999-2000); GDP at factor cost.
### Appendix Table A2
**The Changing Composition of Service Sector (Constant Prices)**  
(Per cent)

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Source (Basic Data): Central Statistical Organization; New Series (Base: 1999-2000); GDP at factor cost.
### Appendix Table A3

The Changing Composition of Agricultural and Allied Activities and Industry Sectors (Current Prices)

(Percent)

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Source (Basic Data): Central Statistical Organization; New Series (Base: 1999-2000); GDP at factor cost.
## Appendix Table A4
The Changing Composition of Service Sector (Current Prices) (Percent)

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<th>Years</th>
<th>Service</th>
<th>Construction</th>
<th>Trade, Hotels, Transport and Communication</th>
<th>Financing, Insurance, Real Estate and Business services</th>
<th>Community, Social, and Personal Services</th>
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### Report of the Commission on Centre-State Relations

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Source (Basic Data): Central Statistical Organization; New Series (Base : 1999-2000); GDP at factor cost.
## Appendix Table A5
### VAT Rates in EU Countries

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<td>USt.</td>
<td>Umsatzsteuer</td>
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<td>Belasting over de toegeweegde waarde</td>
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<td>TVA</td>
<td>Taxe sur la Valeur Ajoutée</td>
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<td>Mehrwertsteuer</td>
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<td>9%</td>
<td>DPH</td>
<td>Daò z poidané hodnoty</td>
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<td>Mervårdagift</td>
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<td>km</td>
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<td>Arvonlisävero</td>
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<tr>
<td>Greece</td>
<td>19%</td>
<td>9% or 4.5%</td>
<td></td>
<td>általános forgalmi adó</td>
</tr>
<tr>
<td></td>
<td></td>
<td>(reduced by 30% to 13%, 6% and 3% on islands)</td>
<td></td>
<td></td>
</tr>
<tr>
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<td>20%</td>
<td>5%</td>
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<tr>
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<td>13.5%, 4.8%</td>
<td>CBL</td>
<td>Cán Bhreisluacha (Irish)</td>
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<td></td>
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<td>or 0%</td>
<td>VAT</td>
<td>Value Added Tax (English)</td>
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<td>Pievienotás vçrtîbas nodoklis</td>
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<td>12% or 5%</td>
<td>IVA</td>
<td>Imposto sobre o Valor Acrecentado</td>
</tr>
<tr>
<td>Madeira and Azores</td>
<td>15%</td>
<td>8% or 4%</td>
<td>IVA</td>
<td>Imposto sobre o Valor Acrecentado</td>
</tr>
<tr>
<td>Romania</td>
<td>19%</td>
<td>9%</td>
<td>TVA</td>
<td>Taxa pe valoarea adaugată</td>
</tr>
<tr>
<td>Slovakia</td>
<td>19%</td>
<td>10%</td>
<td>DPH</td>
<td>Daò z pridané hodnoty</td>
</tr>
<tr>
<td>Slovenia</td>
<td>20%</td>
<td>8.50%</td>
<td>DDV</td>
<td>Davek na dodano vrednost</td>
</tr>
<tr>
<td>Spain</td>
<td>16%</td>
<td>7% or 4%</td>
<td>IVA</td>
<td>Impuesto sobre el valor añadido</td>
</tr>
<tr>
<td>Canary Islands</td>
<td>5%</td>
<td>0% or 2%</td>
<td>IGIC</td>
<td>Impuesto General Indirecto Canario</td>
</tr>
<tr>
<td>Sweden</td>
<td>25%</td>
<td>12% or 6%</td>
<td>Moms</td>
<td>Mervårdesskatt</td>
</tr>
<tr>
<td>United Kingdom</td>
<td>17.50%</td>
<td>5% or 0%</td>
<td>VAT</td>
<td>Value Added Tax</td>
</tr>
</tbody>
</table>

### Appendix Table A5
VAT/GST Rates in Non-EU Countries

<table>
<thead>
<tr>
<th>Country</th>
<th>Standard rate</th>
<th>Reduced rate</th>
<th>Local Name</th>
</tr>
</thead>
<tbody>
<tr>
<td>Albania</td>
<td>20%</td>
<td>0%</td>
<td><strong>TVSH</strong> = Tatimi mbi Vleren e Shtuar</td>
</tr>
<tr>
<td>Argentina</td>
<td>21%</td>
<td>10.5% or 0%</td>
<td><strong>IVA</strong> = Impuesto al Valor Agregado</td>
</tr>
<tr>
<td>Armenia</td>
<td>20%</td>
<td>0%</td>
<td><strong>AAH</strong> = Avelatsvats arjheki hark</td>
</tr>
<tr>
<td>Australia</td>
<td>10%</td>
<td>0%</td>
<td><strong>GST</strong></td>
</tr>
<tr>
<td>Barbados</td>
<td>15%</td>
<td></td>
<td><strong>VAT</strong> = Value Added Tax</td>
</tr>
<tr>
<td>Bosnia and Herzegovina</td>
<td>17%</td>
<td></td>
<td><strong>PDV</strong> = porez na dodatu vrijednost</td>
</tr>
<tr>
<td>Brazil</td>
<td>12%</td>
<td>0%</td>
<td>*IPI - 12% = Imposto sobre produtos industrializados (Tax over industrialized products) - Federal Tax</td>
</tr>
<tr>
<td></td>
<td>+ 25%</td>
<td></td>
<td><strong>ICMS</strong> - 25% = Imposto sobre circulacao e servicos (Tax over commercialization and services) - State Tax</td>
</tr>
<tr>
<td></td>
<td>+ 5%</td>
<td></td>
<td><strong>ISS</strong> - 5% = Imposto sobre servico de qualquer natureza (Tax over any service) - City tax</td>
</tr>
<tr>
<td>Canada</td>
<td>5%</td>
<td>4.50%</td>
<td><strong>GST</strong> = Goods and Services Tax, <strong>TPS</strong> = Taxe sur les produits et services, <strong>HST</strong> = Harmonized Sales Tax, <strong>TVH</strong> = Taxe de vente harmonisie</td>
</tr>
<tr>
<td>Chile</td>
<td>19%</td>
<td></td>
<td><strong>IVA</strong> = Impuesto al Valor Agregado</td>
</tr>
<tr>
<td>Colombia</td>
<td>16%</td>
<td></td>
<td><strong>IVA</strong> = Impuesto sobre el Valor Agregado</td>
</tr>
<tr>
<td>People's Republic of China</td>
<td>17%</td>
<td>6% or 3%</td>
<td><strong>PDV</strong> = porez na dodatu vrijednost</td>
</tr>
<tr>
<td>Croatia</td>
<td>22%</td>
<td>10%</td>
<td><strong>ITBIS</strong> = Impuesto sobre Transfierenca de Bienes Industrializados y Servicios</td>
</tr>
<tr>
<td>Dominican Republic</td>
<td>16%</td>
<td>12% or 0%</td>
<td><strong>IVA</strong> = Impuesto al Valor Agregado</td>
</tr>
<tr>
<td>Ecuador</td>
<td>12%</td>
<td></td>
<td><strong>GST</strong> = Goods and Sales Tax</td>
</tr>
<tr>
<td>Egypt</td>
<td>10%</td>
<td></td>
<td><strong>IVA</strong> = Impuesto al Valor Agregado</td>
</tr>
<tr>
<td>El Salvador</td>
<td>13%</td>
<td></td>
<td><strong>IVA</strong> = Impuesto al Valor Agregado</td>
</tr>
<tr>
<td>Fiji</td>
<td>12.50%</td>
<td>0%</td>
<td><strong>VAT</strong> = Value Added Tax</td>
</tr>
<tr>
<td>Georgia</td>
<td>18%</td>
<td>0%</td>
<td><strong>DGbG</strong> = Dapatetbuli Gbirenekobisi ghasakhadi</td>
</tr>
<tr>
<td>Guatemala</td>
<td>12%</td>
<td></td>
<td><strong>IVA</strong> = Impuesto al Valor Agregado</td>
</tr>
<tr>
<td>Guyana(6)</td>
<td>16%</td>
<td>0%</td>
<td><strong>VAT</strong> = Value Added Tax</td>
</tr>
<tr>
<td>Iran</td>
<td>3%</td>
<td></td>
<td><strong>VAT</strong> = Value Added Tax</td>
</tr>
<tr>
<td>Iceland</td>
<td>24.50%</td>
<td>7%</td>
<td><strong>VSK</strong></td>
</tr>
<tr>
<td>Country</td>
<td>Rate</td>
<td>Other Rates</td>
<td>Notes</td>
</tr>
<tr>
<td>------------------</td>
<td>------</td>
<td>-------------</td>
<td>--------------------------------------------</td>
</tr>
<tr>
<td>India</td>
<td>12.50%</td>
<td>4%, 1%, or 0%</td>
<td>VAT = Valued Added Tax</td>
</tr>
<tr>
<td>Indonesia</td>
<td>10%</td>
<td>5%</td>
<td>PPN = Pajak Pertambahan Nilai</td>
</tr>
<tr>
<td>Israel</td>
<td>15.50%</td>
<td></td>
<td>Ma’am = iñ ññ ññññññ</td>
</tr>
<tr>
<td>Japan</td>
<td>5%</td>
<td></td>
<td>Consumption tax</td>
</tr>
<tr>
<td>South Korea</td>
<td>10%</td>
<td></td>
<td>VAT</td>
</tr>
<tr>
<td>Jersey</td>
<td>3%</td>
<td></td>
<td>GST = Goods and Sales Tax</td>
</tr>
<tr>
<td>Jordan</td>
<td>16%</td>
<td></td>
<td>GST = Goods and Sales Tax</td>
</tr>
<tr>
<td>Kazakhstan</td>
<td>13%</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Kosovo</td>
<td>16%</td>
<td></td>
<td>TVSH - Tatimi mbi Vlerën e Shtuar</td>
</tr>
<tr>
<td>Lebanon</td>
<td>10%</td>
<td></td>
<td>TVA = Taxe sur la valeur ajoutée</td>
</tr>
<tr>
<td>Moldova</td>
<td>20%</td>
<td>5%</td>
<td></td>
</tr>
<tr>
<td>Macedonia</td>
<td>18%</td>
<td>5%</td>
<td></td>
</tr>
<tr>
<td>Malaysia</td>
<td>5%</td>
<td></td>
<td>GST = Goods and Services Tax (Government Tax)</td>
</tr>
<tr>
<td>Mexico</td>
<td>15%</td>
<td>0%</td>
<td>IVA = Impuesto al Valor Agregado</td>
</tr>
<tr>
<td>Montenegro</td>
<td>17%</td>
<td></td>
<td>PDV = Porez na dodatu vrijednost</td>
</tr>
<tr>
<td>New Zealand</td>
<td>12.50%</td>
<td></td>
<td>GST</td>
</tr>
<tr>
<td>Norway</td>
<td>25%</td>
<td>14% or 8%</td>
<td>MVA = Merverdijav (bokmål) or meirverdijav (nynorsk) (informally moms)</td>
</tr>
<tr>
<td>Pakistan</td>
<td>16%</td>
<td>1% or 0%</td>
<td></td>
</tr>
<tr>
<td>Panama</td>
<td>5%</td>
<td></td>
<td>ITBMS = Impuesto de Transferencia de Bienes Muebles y Servicios</td>
</tr>
<tr>
<td>Paraguay</td>
<td>10%</td>
<td>5%</td>
<td>IVA = Impuesto al Valor Agregado</td>
</tr>
<tr>
<td>Peru</td>
<td>19%</td>
<td></td>
<td>IGV = Impuesto General a la Ventas</td>
</tr>
<tr>
<td>Philippines</td>
<td>12%</td>
<td></td>
<td>RVAT = RVAT or Reformed Value Added Tax, locally known as Karagdagang Buwis</td>
</tr>
<tr>
<td>Russia</td>
<td>18%</td>
<td>10% or 0%</td>
<td></td>
</tr>
<tr>
<td>Serbia</td>
<td>18%</td>
<td>8% or 0%</td>
<td>PDV = Porez na dodatu vrednosti</td>
</tr>
<tr>
<td>Singapore</td>
<td>7%</td>
<td></td>
<td>GST</td>
</tr>
<tr>
<td>South Africa</td>
<td>14%</td>
<td>0%</td>
<td>BTW = Belasting op Toegevoegde Waarde, VAT = Valued Added Tax</td>
</tr>
<tr>
<td>Sri Lanka</td>
<td>15%</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Switzerland</td>
<td>7.60%</td>
<td>3.6% or 2.4%</td>
<td>MWST = Mehrwertsteuer, TVA = Taxe sur la valeur ajoutée, IVA = Imposta sul valore aggiunto, TPV = Taglia sin la Plivalur</td>
</tr>
<tr>
<td>Thailand</td>
<td>7%</td>
<td></td>
<td>(Value Added Tax - VAT)</td>
</tr>
<tr>
<td>Trinidad and Tobago</td>
<td>15%</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Turkey</td>
<td>18%</td>
<td>8% or 1%</td>
<td>KDV= Katma deêer vergisi</td>
</tr>
<tr>
<td>Ukraine</td>
<td>20%</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Uruguay</td>
<td>22%</td>
<td>10%</td>
<td>IVA = Impuesto al Valor Agregado</td>
</tr>
<tr>
<td>Vietnam</td>
<td>10%</td>
<td>5% or 0%</td>
<td>GTGT = Giá Trê; Gia Tăng</td>
</tr>
<tr>
<td>Venezuela</td>
<td>9%</td>
<td>8%</td>
<td>IVA = Impuesto al Valor Agregado</td>
</tr>
</tbody>
</table>

Impact of Legal and Jurisprudential Developments in the Last Twenty-Five Years on Centre-State Relations

Study conducted by WBNUJS for the Commission on Centre-State Relations, Government of India
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4. All India Federation of Tax Practitioners and Ors. v. Union of India (UOI) and Ors (1998) 2 SCC 161.
17. Gujarat Ambuja Cements Ltd. and Anr. v. Union of India (UOI) and Anr. AIR 2005 SC 3020.
30. Kulwant Kaur and Ors. v. Gurdial Singh Mann (dead) by Lrs. and Ors. etc., AIR 2001 SC 1273.


34. P.B. Samant v. Union of India 2009(111) BomLR 1745.


39. Rameshwar Prasad and Ors.v. Union of India (UOI) and Anr. AIR 2006 SC 98.


44. Sarbananda Sonowal v. Union of India, AIR 2005 SC 2920.

45. Sapru Jayakar Motilal C.R. Das v. Union of India (UOI) and Ors. AIR1999 Pat 221.


48. Southern Petrochemical Industries Co. Ltd. v. Electricity Inspector and
51. State of Andhra Pradesh and others, etc v. McDowell and Co. and others, etc. AIR1996SC1627.
66. Union of India (UOI) and Ors. v. Shah Goverdhan L. Kabra Teachers College AIR 2002 SC 3675.


71. Yitachu v. Union of India (UOI) and Ors. AIR2008Gau103.
I

Introduction

This study is based on the following three research areas delineated by the Commission on Centre-State Relations:

1. Survey of Supreme Court/High Court decisions in the last twenty-five years to know how the judiciary interpreted Centre-State relations and federalism in India during that period.

2. Study of major developments in respect of Centre-State relations and the principle of federalism in India.

3. Study of the present jurisprudential status of the federal idea in India and distinctions in comparison to the position in 1980s. Any indications of the trends the judiciary is likely to follow or promote in coming years in this regard.

Apart from these three issues, the study also looks at the two other areas of emergency powers and representation of states at the Centre.

In order for the different parts of the study to be coherent, research areas (1) and (3) above have been dealt with in a combined manner in the first part of the report.

Part II deals with legislative developments and Parts III and IV deal with emergency provisions and representations respectively.

The study is descriptive and analytical for the most part. Certain indications alone are made with regard to possible alternatives in parts which deal with unsettled or novel issues.
Study of the Present Jurisprudential Status of the Federal Idea in India and Future Trends of the Judiciary

1. Introduction

1. Federalism, according to K.C. Wheare, is “the method of dividing powers so that the general and regional governments are each, within a sphere, coordinate and independent”.¹ Three rules identify a federal system:

   (1) two levels of government rule the same land and people;

   (2) each level has at least one area of action in which it is autonomous; and

   (3) there is some guarantee (even if merely a statement in the Constitution) of the autonomy of each government in its own sphere.²

2. The restrictive definition of federalism mandates that powers attributed to either level of government are generally exclusively reserved for these levels of government, in theory as well as in practice.³ As noted by Goda Raghuram, J. in a unanimous decision by the Andhra Pradesh High Court, “[t]he inherent corollary of such exclusivity is that if the Parliament or the Legislature of a State fails to legislate, at all or to the full limit of its power, such failure does not have the effect of augmenting the powers of the other level of Government.”⁴

3. As provided by the concurrent list of powers contained in India’s Constitution, India’s situation is slightly different: both Union and States have the power to legislate over certain areas. The details of this arrangement will be

³ Other less restrictive definitions of federalism accept substantial interference by one level of government into the affairs of the other.
discussed below. However, the fact that this list is limited, along with the presence of exclusive lists for the Union and the States, suggests that India, notwithstanding a few eccentricities, fits the definition of a federal country.

4. For William Riker, federalism’s central role is to aggregate the citizens of a large country under one single government. In this way, federalism replaces the empire as the primary means of aggregating large landmasses. For Malcolm Feeley and Edward Rubin, federalism’s central (and ultimately tragic role) is to palliate identity conflicts between groups that cannot agree to a single government, or to “reflect and accommodate these tensions within the broader polity.” Political leaders opt for federalism as a mode of internal organization as “an alternative to dissolution, civil war, or other manifestations of a basic unwillingness of the people in some geographic area within the nation to live under the Central Government.” Barry Friedman perceives many administrative benefits to federalism, which attempts simultaneously to gain the best of power centralisation and decentralisation. On the one hand, centralized authority can provide numerous economic benefits (generally related to efficiency). It may also be appropriate to deal with fundamental rights at the national level. On the other hand, diffusing power in certain circumstances can increase public participation in democracy and government accountability. It can push states to act as laboratories for experimentation. It can protect the health, safety, welfare, and diversity of citizens. Federalism advocates have also long argued that diffusing power, for example through federalism, protects liberty. The goal of federalism should be to maximize the benefits of both centralization and decentralization.

5. Size, identity and democratic or administrative benefits all played a role in the construction of India as a federal country. They also played a role in the actual division of powers between Union and States. The Framers of the Indian

---

5 Riker, supra n.2, at 2-5. Also see Arend Lijphart, Patterns of Democracy: Government Forms and Performance in Thirty-Six Countries (New Haven: Yale University Press, 1999) at 202-203, who notes that the thirteen democracies with unicameral Parliaments in 1996 were small countries: Greece, with a population of slightly more than ten million, was the largest. Riker, Federalism, also argues that centralized federalism, particularly, is generally founded with regards to military goals (at 17-25).
7 Ibid.
10 Barry Friedman, supra n. 8; Feeley and Rubin, supra n.6, would reply that these alleged benefits of federalism are actually benefits of consociation or decentralization (see ch. 1).
11 See e.g., James Madison, The Federalist #62.
12 Barry Friedman, supra n.8.
Constitution sought to strike the appropriate balance between both levels of government. As identity and democratic or administrative benefits in India constantly evolve, they continue to influence the direction of Indian federalism. And because India itself has continued to evolve, its federalism may be outdated; it might no longer work.

6. This study takes an empirical look at Indian federalism by demonstrating the way that courts – often motivated by policy concerns and keenly aware of the Indian Constitution’s failings – have applied and interpreted Indian federalism and managed the relationship between the Union and the States over the years. The study also looks more generally at recent legal developments (while occasionally glancing at political issues) to track where Indian federalism is heading. This study, ultimately, aims to serve as a piece of the puzzle that will allow the government to revise or update Indian federalism, according to its needs. In this light, the study also makes recommendations to improve Indian federalism, based on its empirical findings.

2. Federalism as Perceived by the Supreme Court of India

7. The Supreme Court of India (‘the Court’) has on many occasions explained the nature of the concept of federalism in general and Indian federalism in particular. Post 1985, one of the most significant judicial developments with regard to Indian federalism has been the inclusion of federalism into the basic features of the Indian Constitution.\(^\text{13}\) Being a basic feature of the Constitution does not however elucidate the meaning of the concept of federalism. It only provides it a higher Constitutional status. The conferring of this status reflects the importance that the Court attaches to the idea of federalism in the context of the Constitution.

8. Though there has been a radical change in the status accorded to federalism, there has not been any major change in what the Courts have held federalism to mean. This is not to say that there has been no change in the manner in which the Courts have decided on specific issues involving questions related to federalism. As will be demonstrated in the subsequent sections of this study, certain patterns appear in the way the Supreme Court has ruled on particular issues related to federalism.

9. This section only delineates those features that the Courts in India have held to be hallmarks of Indian federalism. Though the Supreme Court has said that definitional questions concerning federalism do not hold much value for de-

\(^{13}\) S.R. Bommai v. Union of India (1994) 3 SCC 1.
ciding immediate issues before the Court,\(^{14}\) such issues at least demonstrate the perspective from which the Court views Centre-State relations. This would undoubtedly have a bearing on how the Court decides specific cases involving Centre-State and inter-state issues.

a. **Two sets of governments with coordinate spheres of jurisdiction delineated by the Constitution**

10. The Court has consistently held that the hallmark of federalism is the partitioning of power between two sets of government, each government being independent of the other in its respective sphere.\(^{15}\) It grounds this view in the speech of Dr. B.R. Ambedkar in the Constituent Assembly where he sought to defend the federal character of the Indian Constitution in the following words:

There is only one point of Constitutional import to which I propose to make a reference. A serious complaint is made on the ground that there is too much of centralization and that the States have been reduced to Municipalities. It is clear that this view is not only an exaggeration, but is also founded on a misunderstanding of what exactly the Constitution contrives to do. As to the relation between the Centre and the States, it is necessary to bear in mind the fundamental principle on which it rests. The basic principle of Federalism is that the legislative and executive authority is partitioned between the Centre and the States not by any law to be made by the Centre but the Constitution itself. This is what the Constitution does. The States, under our Constitution, are in no way dependent upon the Centre for their legislative or executive authority. The Centre and the States are co-equal in this matter. It is difficult to see how such a Constitution can be called centralism. It may be that the Constitution assigns to the Centre too large a field for the operation of its legislative and executive authority than is to be found in any other Federal Constitution. It may be that the residuary powers are given to the Centre and not to the States. But these features do not form the essence of federalism. The chief mark of federalism, as I said lies in the partition of the legislative and executive authority between the Centre and the Units by the Constitution. This is the principle embodied in our Constitution.”

\(^{14}\) “For our purpose, further it is really not necessary to determine whether, in spite of the provisions of the Constitution referred to above, our Constitution is federal, quasi- federal or unitary in nature. It is not the theoretical label given to the Constitution but the practical implications of the provisions of the Constitution which are of importance to decide the question that arises in the present context” S.R. Bommai v. Union of India (1994) 3 SCC 1.

\(^{15}\) See Kuldeep Nayar v. Union of India (2006) 7 SCC 1, State of Andhra Pradesh and others, etc. v. McDowell and Co. and others, etc. AIR 1996 SC 1627, i, supra n. 13, para. 363.
This line of argument satisfies basic definitional issues, but questions arise again when one refers to a host of other factors including provisions of the Constitution dealing with repugnancy between Union and State laws, emergency powers, the role of the Governor, legislations on national security and the circumstances under which the Central Government can make laws on State subjects. The Court has dealt with such questions by employing various interpretative materials and strategies to add substantially to Dr. Ambedkar's basic definition.

11. The other essential feature of federalism, according to the Court, is the fact that the powers of the two sets of government are delineated by the Constitution:

“The distribution of the legislative and executive power within limits and coordinate authority of different organs are delineated in the organic law of the land, namely the Constitution itself. The essence of the federalism, therefore, is distribution of the force of the state among its coordinate bodies. Each is organised and controlled by the Constitution...."\(^{16}\)

This view is in line with the view expressed by the Supreme Court in *State of West Bengal v. Union of India* AIR1963 SC 1241 where the Court had held:

“Under the Constitution of India the political sovereignty is divided between the constitutional entities, that is, the Union and the States, who are juristic personalities possessing properties and functioning through the instrumentalities created by the Constitution. The Indian Constitution accepts the federal concept and distributes the sovereign powers between the coordinate constitutional entities, namely, the Union and the states.”

In this way, Indian courts have defined federalism consistently with William Riker's longstanding general definition for federalism.\(^{17}\)

b. **A model of federalism rooted in Indian history and realities**

12. The decisions of the Court consistently argue that the Indian Constitution is federal, although it does not fully conform to traditional models of federalism

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\(^{16}\) S.R. Bommai, supra n. 13, at para 248.

\(^{17}\) Riker, supra n. 2, at 11.

\(^{14}\) In S.R. Bommai v. Union of India (1994) 3 SCC 1, the Supreme Court stated:

“53. The expression “Federation” or “federal form of government” has no fixed meaning. It broadly indicates a division of powers between a central (federal) government and the units (States) comprised therein. No two federal Constitutions are alike. Each of them, be it of U.S.A., Canada
like in the United States of America. In *S.R. Bommai v. Union of India*, the Court argued that India cannot be slotted into any one kind of federal model.\textsuperscript{18} It is a unique federal model which is sensitive to its needs and rooted in its history: “...federalism in the Indian Constitution is not a matter of administrative convenience, but one of principle, the outcome of our own historical process and a recognition of the ground realities.”\textsuperscript{19}

13. The Court recognises the historical reality that unlike in the United States, the federal units in India did not come together to form a state.\textsuperscript{20} References to the debates of the Constituent Assembly, which in turn refer to the Government of India Act, 1935, clearly demonstrate the continuity that the Constitution makers maintained with earlier laws while distributing powers between the States and the Centre. Surprisingly, maintaining this continuity coincided with other values held by many influential members of the Constituent Assembly, the dominant value being the unity and integrity of the country. This was cited by many members of the Constituent Assembly as a reason to have a strong Central Government.\textsuperscript{21} Many others however regarded this continuity and centralisation as reasons for denying the claim that the Indian Constitution was truly federal.\textsuperscript{22} Eventually the strong Centre model prevailed as the amendments moved for lesser powers to the Centre were not adopted.

14. The provisions establishing a strong Centre have been justified on a number of grounds, the prominent ones being: that they come into operation only in unusual circumstances, that such provisions exist in other federal Constitutions as well and that they are necessary for maintaining the unity and territo-

\textsuperscript{19} *S.R. Bommai*, supra n. 13;
\textsuperscript{20} *The Constitutional culture and political morality based on healthy conventions are the fruitful soil to nurture and for sustained growth of the federal institutions set down by the Constitution. In the context of the Indian Constitution federalism is not based on any agreement between federating units but one of integrated whole as pleaded with vision by Dr. B.R. Ambedkar on the floor of the constituent assembly at the very inception of the deliberations and the Constituent Assembly unanimously approved the resolution of federal structure. He poignantly projected the pitfalls flowing from the word “federation”.*
\textsuperscript{21} For a sample of such arguments with regard to the governor’s discretionary powers during emergencies, see, *Constituent Assembly Debates, Vol.4, proceedings of Wednesday, the 23rd JULY, 1947.*
rial integrity of the country. The argument based on the territorial integrity was made by citing serious threats in the country and abroad prevalent at the time when the Constitution was being drafted.23

15. While referring to the unique features of Indian federalism, the Court has chosen to point out that these features made the Constitution “both unitary as well as federal according to the requirement of time and circumstances”.24 This seems to portray the centralising features as desirable ones. Surprisingly, the Court also quotes Dr. Ambedkar to show that the Constitution makers hoped that features of the Constitution like the emergency provisions would seldom be brought into use.25 These two seemingly opposing views on the provisions like the emergency powers can be explained by the constant tension that exists between instrumental benefits of centralised coordination and the right of nationalities and communities to decide for themselves. This latent tension is sought to be reconciled by the Court by explaining the logic of the distribution of powers between the Centre and the States. The logic being, that matters of national importance are to be dealt with by the Central Government while those of local interest are to be dealt with by the State Governments.26

c. A federal state with a strong Centre

16. The Supreme Court has stated that the Constitution makers have intended India to be a federal state with a strong Centre.27 Though the State and the

23 Ibid.
24 S.R. Bommai, supra n. 13, at para 253, quoting Dr. Ambedkar from the Constituent Assembly Debates.
25 The court quoted Dr. Ambedkar to substantiate this claim: “In fact I share the sentiments expressed...that the proper thing we ought to expect is that such Articles will never be called into operation and that they will remain a dead letter. If at all, they are brought into operation, I hope the President who is endowed with all these powers will take proper precautions before actually suspending the administration of the provinces. I hope the first thing he will do would be to issue a clear warning to a province that has erred that things were not happening in the way in which they were intended to happen in the Constitution.” S.R. Bommai, supra n. 13, at para 360.
26 In S.R. Bommai, supra n. 13 the Court stated:
“248. The federal state is a political convenience intended to reconcile national unity and integrity and power with maintenance of the state’s right. The end aim of the essential character of the Indian federalism is to place the nation as a whole under control of a national Government, while the States are allowed to exercise their sovereign power within its legislative and co-extensive executive and administrative sphere. The common interest is shared by the Centre and the local interests are controlled by the State....253. In the State of West Bengal v. Union of India, (2004)10 SCC 201, this Court laid emphasis that the basis of distribution of powers and between Union and the States is that only those powers and authorities, which are concerned with the regulation of local problems are vested in the State and those which tend to maintain the economic nature and commerce, unity of the nation are left with the Union.”
Central Governments are sovereign in their respective spheres, the bias towards the Centre is clear from various provisions of the Constitution. “(The) Tilt in favour of the Centre is required to be construed having regard to the importance of the subject matter of Parliamentary legislation and the impact and practical effect of the in-road of the State Laws entrenching upon the legislative field occupied by the Parliament.”

17. The contours of this bias are however unclear. Subsequent decisions of the Court have stated that the federal nature of the Constitution demands an interpretation that does not whittle down the powers of the States.

d. Federalism as an instrument for attaining larger substantive goals

18. Though the Supreme Court has defined federalism in terms of a dual sovereignty model, it has on some occasions attributed certain substantive goals that federalism has been designed to serve. For example in *S.R. Bommai* Justice Ramaswamy was of the opinion:

“243. The polyglot Indian society of wide geographical dimensions habit ing by social milieu, ethnic variety or cultural diversity, linguistic multiplicity, hierarchical caste structure among Hindus, religious pluralism, majority of rural population and minority urban habitus, the social and cultural diversity of the people furnish a manuscript historical material for and the founding fathers of the Constitution to lay federal structure as foundation to integrate India as an united Bharat. Federalism implies mutuality and common purpose for the aforesaid process of change with continuity between the Centre and the States which are the structural units operating on balancing wheel of concurrence and promise to resolve problems and promote social, economic and cultural advancement of its people and to create fraternity among the people.

[…]

253. As earlier stated, the organic federalism designed by the founding fathers is to suit the Parliamentary from of Govt., to suit the Indian conditions with the objective of promoting mutuality and common purpose rendering social, economic and political justice, equality of status and opportunity; dignity of person to all its citizens transcending re-

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27 See S.R. Bommai, supra n. 13; Kuldeep Nayyar supra n. 19; *Automobile Transport (Rajasthan) Ltd. v. The State of Rajasthan & Ors.*, 1962 (1) SCR 491.
29 Kuldeep Nayyar, supra n. 19.
regional, religious, sectional or linguistic barriers as complimentary units in working the Constitution without confrontation. Institutional mechanism aimed to avoid friction to promote harmony to set Constitutional culture on firm foothold for successful functioning of the democratic institutions, to bring about matching political culture adjustment and distribution of the roles in the operational mechanism are necessary for national integration and transformation of stagnant social order into vibrant egalitarian social order with change and continuity economically, socially and culturally.”

The substantive goals discussed by the Court hold great potential in terms of providing indicators as to what principles of interpretation should be followed while dealing with matters involving Centre-State relations. The role of these substantive goals and Constitutional values has not been explored by the Supreme Court. The two exceptions are the unity and integrity of the country and the benefit of a coordinated economy. These two however are arguably instrumental reasons rather than substantive goals in themselves.

e. Federalism demands interpretation that does not whittle down the power of the States

19. In Kuldeep Nayyar v. Union of India\[30\] the Court held that the States were not mere appendages of the Centre. It further stated that there is a delicate balance created by the Constitution between the powers of the Centre and the States. This balance was not to be upset by the Court. In the words of the Court:

“The fact that under the scheme of our Constitution, greater power is conferred upon the Centre vis-à-vis the States does not mean that States are mere appendages of the Centre. Within the sphere allotted to them, States are supreme. The Centre cannot tamper with their powers. More particularly, the Courts should not adopt an approach, an interpretation, which has the effect of or tends to have the effect of whittling down the powers reserved to the States...must put the Court on guard against any conscious whittling down of the powers of the States. Let it be said that the federalism in the Indian Constitution is not a matter of administrative convenience, but one of principle the outcome of our own histori-

\[30\] Supra n. 19 at para 276.
This reasoning suggests that in order to maintain the delicate balance created by the Constitution, it is important to adopt principles of interpretation that do not whittle down the powers of the States. An approach in favour of protecting the powers of the States had earlier been adopted in cases like *State of Andhra Pradesh and others etc. v. McDowell & Co. and others*. In that case the Supreme Court held that the scope of Article 254 and the doctrine occupied field really applied only to matters under the concurrent list.

20. It is interesting to contrast the observations in *Kuldeep Nayyar* with those in *State of West Bengal v. Kesoram Industries*. In *Kesoram* the Court clearly stated that the “(T)ilt in favour of the Centre is required to be construed having regard to the importance of the subject matter of Parliamentary legislation and the impact and practical effect of the in-road of the State Laws entrenching upon the legislative field occupied by the Parliament”32. “It would therefore, not be correct for the superior courts to advocate the theory that while interpreting the Constitution, courts should lean in favour of the State. Federal character of the Union of States in India does not support the said theory.”33

21. The later decision in *Kuldeep Nayyar* seems to state exactly the opposite. Yet both judgments justify their positions on the basis of the federal character of the Indian Constitution. It can however be argued that the Court in *Kuldeep Nayyar* does not advocate a theory in favour of the States. Rather it prescribes interpretations that do not whittle down the power of the States, the powers being prescribed by the Constitution. *Kesoram* prescribes that “(t)he interpretive principles whether leaning in favour of the Union or the State may, in certain situations, depend upon the subject matter of legislation, the importance thereof and its effect and impact within and outside the country. Both mineral and tea deserve more control only by the Union having regard to their importance in national economy.”34 This is to be contrasted to para. 228 where the Court states: “The doctrine of federalism in the Indian context would

32 Kesoram, supra n. 28, at para 229.
34 Ibid, at para 260.
mean proper and effective interpretation of the Constitution in respect whereof political or economic views have no role to play."

22. The Court in *Kesoram* seems to suggest that interpretive choices are to be made based on the provisions of the Constitution, which inevitably involves considering the consequences of such interpretations on the country and abroad. Though the judgment does not seem to be completely coherent in its statement of criteria governing interpretive choices, it should at least not be considered as one that advocates interpretations in favour of the Centre. This is so because the judgment also holds that when necessary the States could also be favoured:

> The Constitution is an organic living document. Its outlook and expression as perceived and expressed by the interpreters of the Constitution must be dynamic and keep pace with the changing times. Though the basics and fundamentals of the Constitution remain unalterable, the interpretation of the flexible provisions of the Constitution can be accompanied by dynamism and lean, in case of conflict, in favour of the weaker or the one who is more needy.\(^\text{35}\)

Considering these judgments, it seems that the decision of the Court in *Kuldeep Nayar* is not inconsistent with earlier positions. Rather it builds on the earlier judgments which highlight the dynamic nature of the Constitution.

### 3. High Court Cases

23. Given the unified structure of the judiciary in India, it is improbable that the law laid down by the High Courts would be different from that of the Supreme Court. It is however possible to identify certain dominant themes in the decisions of the High Courts, much of which would inevitably reflect the position taken by the Supreme Court. In this section we survey decisions of the High Courts with an eye on spotting such recurrent themes.

a. **Preserving the power of the States in a federal polity in spite of a bias towards the Centre**

24. Most High Court decisions reflect the position of the Supreme Court that though our Constitutional framework envisages a bias towards the Centre, it is necessary to preserve the powers of the State within their respective spheres.

\(^{35}\) Ibid, at para 50.
The States are not the agents of the Centre and the federal nature of the Constitution requires that the power of the States is in no way constitutionally denuded.

25. In Goel Bus Service v. State of H.P. and Ors\(^36\) it was held that “The federal nature of the Constitution demands that an interpretation which would allow the exercise of legislative power by Parliament pursuant to the residuary powers vested in it to entrench upon State legislation and which would thereby destroy or belittle State autonomy must be rejected.” The case dealt with the conditions under which Entry 97 of List I could be invoked. The Court held that before exclusive legislative competence is claimed for Parliament by resort to its residuary power, the legislative incompetence of the State Legislature must be clearly established. The words of Entry 97 made it explicit that the Entry could be resorted to only if the field of legislation in question is not enumerated in List II or List III. In cases where the competing Entries are an Entry in List II and Entry 97 of List I, the Entry in the State List must be given a “broad and plentiful” interpretation.

26. In A.P. TRANSCO v. Sri Gouri Sankar Cable Industries and Ors\(^37\) the Andhra Pradesh High Court held that the Supreme Court has interpreted that India has a federal polity. Each State has independent Constitutional existence assigned with an important political role. States though not separate sovereigns, neither Union nor States possess untrammelled sovereignty because the legislative, executive and judicial powers in India are divided between the Union and the States.\(^38\)

27. In some cases, High Courts have even construed the powers of the States in a manner which required the Central Government to take permission from the State to legislate on certain matters.\(^39\)

28. Though these decisions seem to indicate that the powers of the States ought to be preserved, there have been other High Court decisions which clearly


\(^{37}\) 2002(3) ALT 134.


\(^{39}\) See Indumati M. Shab and Ors. v. Narendra Muljibhai Aera and Ors., 1995 CriLJ 918, where the Court said that the essence of federalism is that the Central Government has to obtain consent of the State Government if it has to exercise its police powers under the Delhi Special Police Establishment within the territory of a State.
recognise the bias towards the Centre in the Indian Constitution. In Advocate General, Andhra Pradesh, Hyderabad v. Rachapudi Subba Rao⁴⁰ the Court referred to Dr. Ambedkar’s speeches in the Constituent Assembly Debates, K. C. Wheare’s theory on federalism, Rajmannar Committee’s report on the Centre-State Relations, and almost all important cases dealing with federalism. Rooting itself in the historical context of the Constituent Assembly, it held that the present federal structure tilting in favour of a strong Centre reflects the overwhelming desire and determination of the Founding Fathers to preserve the unity and territorial integrity of the nation. This prevented the Indian Constitution from adhering to the essential feature of traditional federalism, namely agreement between the federal Union and federating States to come together as one single unit. The Court was however careful to add that though the Constitution inclines in favour of a strong Centre, its federal character, as it obtains today, cannot be destroyed or abrogated.

29. In P.B. Samant v. Union of India⁴¹ following the observations of the Supreme Court in Kuldeep Nayar and Kesornam Industries, the Court said that

“though the federal principle is dominant in our Constitution ...it is also equally true that federalism under the Indian Constitution leans in favour of a strong Centre, a feature that militates against the concept of strong federalism. .... In addition to these principles, it is a settled cannon of Constitutional law that the law enacted by Union Parliament will have precedence over the State laws wherever they operate in the same field. This being the Constitutional scheme and Jawaharlal Nehru National Urban Renewal Mission having been considered as national policy, it can hardly be contended that it was a temptation offered by the Union which tantamounts to exercising of undue influence or arbitrariness in relation to the affairs of the State Government and the State Legislative Assembly.”⁴²

These decisions indicate that the position of the High Courts has been similar to that of the Supreme Court with regard to the nature of Indian federalism. It can however safely

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⁴⁰ 1991Cri LJ 613.
⁴¹ 2009(111) Bom LR 1745
be said that most High Court decisions do not fail to state the importance of preserving the power of the States and there seems to be no disagreement in this regard, unlike in the case of the decisions of the Supreme Court.

b. Cooperative Federalism

30. Many High Court decisions have described the Indian version of federalism as a cooperative one. The existence of concurrent legislative powers is said to be an example of co-operative federalism, which is meant to accommodate and balance the perceptions of both the Union and the State in the field of legislation. The Centre and the States must be presumed to be conscious of the need for accord and need for accommodating interests of each other.  

31. Again in *Halar Utkarsh Samiti and Anr. v. State of Gujarat*, the Court stated that there are no watertight compartments between the spheres of the Central and State executives. In a cooperative federal structure, the interaction between the Central and State executive authorities is essential for good governance.

32. The idea of cooperative federalism was referred to in spite of the Court expressly recognising that the Constitution of India has leaned towards a stronger Union by providing that the executive power of every State shall be so exercised as not to impede the exercise of the executive power of the Union. Further, that the executive power of the Union shall extend to the giving of such directions to a State as may appear to the Government of India to be necessary for that purpose. It was therefore held that there was nothing unusual if the Prime Minister in exercise of the executive power of the Union issues necessary directions to a State, which may be warranted by Articles 256 and 257 of the Constitution. The Prime Minister’s writing to the Chief Minister in connection with the concerned project before any decision was taken on it, thus did not amount to pressurising the State Government.

33. In *Ranga Reddy District Sarpanches’ Association and Ors. v. Government of A.P. and Ors* the Court was of the opinion that Federalism demands a special mode of political and social behaviour, involving a commitment to partnership and active co-operation on the part of individuals and institutions, at the same time preserving their own integrity.

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44 *Special Civil Application No. 7372 of 1999, Gujarat High Court.*
45 2004(1) ALT 659.
“To maintain the federal principle, the general Government and the constituent polities are required to each have their substantially complete governing institutions of their own, with the right to modify these institutions unilaterally within the limits set by the federal compact. It is not necessary that separate institutions of each of the constituting units must carry out all governing activities. The agencies of one unit may serve as agents of the other by mutual agreement or institutional arrangement. However, each unit must have enough of its own institutions to function in the areas of its authority and to co-operate freely with the counter-part agencies.” 46

It was held in this case that in our federal system though the Panchayats are not a part of the federal structure, they nevertheless constitute an integral component of some measure of vertical division of governance power.47 “The Panchayats with the constitutionally defined character of being “self-government”(s) are now legitimate inhabitants of and entitled in their own right to share in some measure, the Constitutional space. The Union and States are required to recognise, respect and enable this spatial freedom and autonomy accorded to these entities under the Constitutional dispensation - post-73rd Amendment.”48

34. In Hotel Dwaraka, Hyderabad v. The Union of India and Ors49, the Court referred to Articles 248, 249, 250, 252, 356, and 357 to indicate that the Indian federation is a flexible one and does not suffer from the twin evils of rigidity and legalism. It is a new kind of federalism, which the Constituent Assembly produced to meet India’s peculiar needs. What is contemplated is co-operative federalism which provides for a strong Central Government. It does not necessarily result in weak provincial governments which are administrative agencies for central policies.

35. According to the Court, Indian federalism reflects real co-operative federalism as the provincial governments have been working in co-operation for implementing the policies and programmes of the Central Government. The key concept of co-operative federalism is partnership locking the States and the Central Government in joint endeavours to pursue commonly shared goals. The Court referred to the Articles of the Constitution to demonstrate that the Constitution envisaged a vertical relationship between the States and the Central Government, with the State Governments having the obligation to com-

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1 Ibid, at para 57.
2 Ibid, at para 119.
3 Ibid, at para 129.
ply with the laws and directions of the Central Government. However, within the Constitutional limits the constituent units can have their own way unless strong case is made to the contrary. The Court concluded that the Indian Constitution does not suffer from rigidity and legalism of federalism, but it is a Constitution having federal structure with unitary features intended to meet the peculiar conditions of India.

c. Broad trends visible in the decisions on federalism by the High Courts

36. The decisions of the High Courts do not differ from those of the Supreme Court in describing the nature of Indian federalism. Predictably, at most instances their decisions follow those of the Supreme Court. However, it could be argued, that the High Courts have continuously stressed on the cooperative nature of Indian federalism. In most decisions the High Court have stressed on this fact, in spite of clearly recognising the unitary bias in the Constitution of India.

37. It can also be safely argued that the idea of unitary bias is not a dominant feature of the High Court decisions. This stands out starkly in contrast to many Supreme Court decisions before S.R. Bommai, which start with the premise of unitary bias and spend considerable lengths of time in proving either the fact of the existence of the bias or its necessity in the context of India. In the High Court decisions however, the limelight is on the cooperative nature of Indian federalism. The fact of the unitary bias is present more in terms of recognition of its existence, which in turn is sensitive to the historical context of the constituent assembly.

38. The other trend identifiable in the High Court decisions is that their vision of cooperative federalism is one where the States have a significant role to play as independent constituent units. The fact of unitary bias does not warrant reducing the role to be played by the States. The area of operation provided to them by the Constitution is to be preserved unless there are strong reasons to the contrary. This view of federalism will presumably have an important bearing on Centre-State issues, as it would play an important role in choosing amongst the various interpretative avenues open to courts while interpreting provisions which are ambiguous.

39. These trends must however be accepted with some caution. The trends do not necessarily lead to the conclusion that the High Courts have developed a  

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1 The Court referred to Articles 256,257 and 365 to support this claim
distinct jurisprudence focusing on cooperative federalism, which reduces the role of the fact of unitary bias. This is because the Supreme Court too has gradually moved away from ascribing a determinative role to the fact of unitary bias in deciding disputes involving Centre-State relations. The High Courts are thus bound to follow suit.

40. The other note of caution arises from the possibility of allegations of cherry picking when spotting trends in High Court decisions. This is especially the case in an area of Constitutional law which has countless decisions to its credit. Making any claims of spotting trends must thus stand up to this allegation on the basis of the strength of its research given its purpose.

41. This study spots the trends mentioned above on the basis of both, cases which discuss federalism generally and spell out its contours in the context of the Indian Constitution and, cases dealing with the Seventh Schedule and emergency provisions, which are discussed in the sections that follow.
Report of the Commission on Centre-State Relations
III

How Has the Judiciary Interpreted Centre-State Relations and Federalism in India since 1985?

1. Roadmap of the Judiciary: Constitutional Intent and Seventh Schedule Distribution of Powers

42. The Framers of the Indian Constitution worked hard to strike the proper balance between Union and State powers. Ultimately, the Framers established the Union Powers Committee, whose second report drew up potential legislative lists and other divisions of powers. While the Committee believed that it would be injurious to India’s health to provide a weak central authority, it also concurred that to frame a Constitution on the basis of a unitary state would be a retrograde step, both politically and administratively. The Committee concluded that the soundest framework for India was a Union of States with a federal Constitution. In this way, the States would have power while the Centre would remain stable and strong. It would be a federal state with a strong Centre. The Committee also recommended that residuary powers under the Constitution should rest with the Centre. The Committee’s decisions were subsequently broadly debated, but ended up forming the backbone of the eventual distribution of powers.\(^51\)

43. Article 246 gives to the Indian Parliament and State Legislatures the power to legislate on the legislative fields contained in the Seventh Schedule.\(^52\) It reads as follows:

246. (1) Notwithstanding anything in clauses (2) and (3), Parliament has exclusive power to make laws with respect to any of the matters enumerated in List I in the Seventh Schedule (in this Constitution referred to as the “Union List”).

(2) Notwithstanding anything in clause (3), Parliament, and, subject to clause (1), the Legislature of any State also, have power to make laws

\(^{51}\) See Constituent Assembly Debates, Vol.5

with respect to any of the matters enumerated in List III in the Seventh Schedule (in this Constitution referred to as the “Concurrent List”).

(3) Subject to clauses (1) and (2), the Legislature of any State has exclusive power to make laws for such State or any part thereof with respect to any of the matters enumerated in List II in the Seventh Schedule (in this Constitution referred to as the “State List”).

(4) Parliament has power to make laws with respect to any matter for any part of the territory of India not included in a State notwithstanding that such matter is a matter enumerated in the State List.

Article 246’s first three clauses demarcate legislative powers between the Parliament and the State Legislatures. Ultimately, Parliament has the exclusive power to legislate with respect to any matter enumerated in List I, the “Union List”, in the Seventh Schedule. Parliament and State Legislatures have the concurrent power to legislate with respect to any matter enumerated in List III of the Seventh Schedule, the “Concurrent List”. State Legislatures have the exclusive power to legislate in respect to any matter enumerated in List II of the Seventh Schedule, the “State List”. Parliament and State Legislatures are each exclusively responsible for a large number of entries, but Parliament is supreme. If any of the entries in the three lists overlap, the entries in List I will prevail. Some entries in the State List are subject to entries in the Union or the Concurrent Lists or to a law made by Parliament, while some entries in the Concurrent List are subject to entries in the Union List or to laws made by Parliament.

2. Survey of the Judiciary’s Decisions on Centre-State Relations Since 1985

a. Scope of powers and principles governing conflicts between Union and States

44. The Indian judiciary’ theoretical approach to federalism is consistent with the practical framework that it has established to deal with federalism, specifically on issues such as the scope of government powers and conflicts between the Union and the States. As stated by Rajeev Dhawan and Rekha

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53 Entries 11, 13, 17, 22, 23, 24, 32, and 54, List II.
54 Entries 11, 13, 26, 27, 57, List II.
55 Entries 12, 37, 50, List II.
56 Entries 19, 32, List III.
57 Entries 31,33(a), 40, List III.
Interpretation of Entries Under the Seventh Schedule

45. The Constitution distributes legislative powers between the Union and the States. The principal distribution is found under Article 246, combined with the Seventh Schedule. The Union can legislate on matters found in Lists I and III of the Seventh Schedule, while the States can legislate on matters found in Lists II and III. List III therefore allows concurrent jurisdiction to the Union and the States. Throughout its jurisprudence since 1985, the Supreme Court of India has emphasized that similarly to the rest of the Indian Constitution, all entries in the Seventh Schedule should be interpreted broadly and liberally, to the maximum extent of their powers. The “widest amplitude” should be given to the various entries. If Entry 66 of List I, for example, allows the Union to legislate on education, this includes all matters related to education. The Supreme Court confirmed in Synthetics and Chemicals Ltd. v. State of U.P., moreover, that “[e]ach general word should be held to extend to all ancillary or subsidiary matters which can fairly and reasonably be comprehended in it.”

46. On the other hand, it is clear that the various entries must be interpreted harmoniously. The broad and liberal interpretation afforded to one Entry must not obliterate another Entry or render it meaningless. Thus, the broad and liberal interpretation “is subject to certain exceptions and a restricted meaning may be given to words if it is necessary to prevent a conflict between two exclusive entries.”

47. In Welfare Asscn. A.R.P., Maharashtra and Anr. v. Ranjit P. Gohil and Ors., the Supreme Court noted that while courts aim to strike a balance between the two factors of interpretation, courts prefer solutions that uphold the ability of a body to legislate: “One bank is the salutary rule that the words conferring

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59 Synthetics and Chemicals Ltd. supra n. 52, at para. 68.
60 Ibid.
the right of the legislation should be interpreted liberally and the powers conferred should be given the widest amplitude; the other bank is guarding against extending the meaning of the words beyond their reasonable connotation in an anxiety to preserve the power to legislate. The working rule of the game is to resolve, as far as possible, in favour of the legislative body any difficulty or doubt in ascertaining the limits.”

48. Because the entries are to be interpreted broadly and liberally, the Supreme Court has been reticent to refer to the residuary powers contained in Article 248 and Entry 97. Since the Union holds all residuary powers, a restraint on the use of these powers has benefited the States. The residuary powers have been exercised a few times, particularly before 1985. For example, in *Second Gift Tax Officer v. D.H. Nazareth*, Hidayatullah, C.J., claimed that a gift tax could be justified under no other entries in the list. Therefore, the power to impose one must lie with the Union through Article 248 read with Entry 97. The residuary powers also justified an expenditure tax in *H.H. Prince Azam Jha Babadur v. Expenditure Tax Officer* and post-1989 in *Federation of Hotel & Restaurant Assn. of India v. Union of India*. In another case, the Supreme Court determined that Entry 97 justified certain provisions of the Income Tax Act, 1961, that enabled the government to borrow from a certain class of taxpayers. Hidayatullah, J., met the majority opinion with a vigorous dissent: he argued instead that the legislation could be validly made under Entry 82 of List I.

49. There may be more references to the residuary powers in the case of taxation disputes, possibly because taxation is more specifically divided throughout the lists. On the whole, however, references to Entry 97 have been very infrequent since 1985. The Supreme Court has refused to expand the powers of the Union in this fashion, maintaining a strong division of powers. As a sign of its concern for States’ powers, the Supreme Court has also recently explicitly stated, for example, that the existence of Entry 97 cannot be used to justify narrowing down an Entry in the State List.

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68 All India Federation of Tax Practitioners and Ors. v. Union of India (UOI) and Ors, (1998) 2 SCC 161 at para. 39; also see Bharat Sanchar Nigam Ltd. and anr. v. Union of India and anr, 2006 (3) SCC 1.
Legislative Incompetence

50. The Union Government is incompetent to legislate on matters contained in List II. List II is out of its jurisdiction. Likewise, the State Government is incompetent to legislate on matters contained in List I. To assess whether or not a government’s legislation is valid, it is necessary to assess if it falls under an Entry where the government is competent to legislate. Consistent with the judiciary’s intention to resolve matters in favour of the body that has legislated, wherever a law is challenged on the ground that it was passed pursuant to an Entry where the government was incompetent to legislate, there is an initial presumption that the law is Constitutional. Moreover, the Court will use every legal effort to ensure the Constitutionality of the law, even if it means going beyond the pleadings of the impugned government. Finally if ever the limit of the legislative power is uncertain, the doubt should be resolved if possible in favour of the legislature. In *State of Bihar v. Bihar Distilleries Limited*, the Supreme Court detailed how to ascertain the Constitutional validity of a provision or law:

“The approach of the Court, while examining the challenge to the constitutionality of an enactment, is to start with the presumption of constitutionality. The court should try to sustain its validity to the extent possible. It should strike down the enactment only when it is not possible to sustain it. The court should not approach the enactment with a view to pick holes or to search for defects of drafting, much less inexactitude of language employed. Indeed, any such defects of drafting should be ignored out as part of the attempt to sustain the validity/ constitutionality of the enactment. After all, an Act made by the legislature represents the will of the people and that cannot be lightly interfered with. The unconstitutionality must be plainly and clearly established before an enactment is declared as void. The same approach holds good while ascertaining the intent and purpose of an enactment or its scope and application....”

51. In the case of a Union law, the Supreme Court often finds it simpler merely to examine whether its subject matter falls under a State power (rather than at-
tempting to ascertain what Union power it falls under). If it falls under a State power, it is invalid. If it does not, by process of elimination, it must be valid.\footnote{As M.P. Singh points out in Constitution of India, at 751, this approach can be dangerous, because the Constitution attributes several other legislative powers to the State, outside of the context of the Seventh Schedule, such as in Article 209: see also State of Punjab v. Satyapal, AIR 1969 SC 903, 914 and M.P. Singh, “Legislative Power in India: Some Clarifications” (1975 & 76) 4 & 5 Delhi L. Rev. 73 at 96.}

In the words of the Supreme Court: “While examining the legislative competence of Parliament to make a law what is required to be seen is whether the subject matter falls in the State List which Parliament cannot enter. If the law does not fall in the State List, Parliament would have legislative competence to pass the law by virtue of the residuary powers under Article 248 read with Entry 97 of the Union List and it would not be necessary to go into the question whether it falls under any Entry in the Union List or the Concurrent List.”\footnote{Naga People’s Movement of Human Rights v. Union of India, (1998) 2 SCC 109: AIR 1998 SC 431 at para. 25; also see Union of India v. H.S. Dhillon, (1971) 2 SCC 779: AIR 1972 SC 1061 at 1078; S.P. Mittal v. Union of India, [1983] 1 S.C.R. 51 and Kartar Singh v. State of Punjab, (1994) 3 SCC 569.}

52. Even where a State law appears to tread into a List I (Union) Entry, or where a Union law appears to tread into a List II (State) Entry, the Supreme Court has determined that laws should not be automatically struck down. This is consistent with its approach of allowing governments to legislate on broad entries. Instead, a court must first assess the “pith and substance” of the act: its true nature. As recognized by the Supreme Court, “[i]f on such an examination it is found that the legislation is in substance one on a matter assigned to the legislature then it must be held to be valid in its entirety even though it might incidentally trench on matters which are beyond its competence.”\footnote{Union of India (UOI) and Ors. v. Shah Goverdhan L. Kabra Teachers College, AIR 2002 SC 3675 at para. 7.}

In other words, if the pith and substance of a State Act resides within a field of State jurisdiction, the law will stand, even if it incidentally treads on a Union Entry; likewise for a Union act that incidentally treads on a State Entry: “The fact of incidental encroachment does not affect the vires of the law even as regards the area of encroachment.”\footnote{P.N. Krishna Lal v. Gov’t of Kerala, (1995) Supp (2) SCC 187 at para. 10.}

53. Of course, the pith and substance test must be applied “to the enactment as a whole, … to its main objects, and … to the scope and effect of its provi-
Moreover, the pith and substance doctrine does not allow a legislature to implement “colourable” legislation, that is, legislation that attempts to do indirectly what a legislature cannot do directly. In fact, the pith and substance doctrine can help to decide where a government is attempting to pass colourable legislation. As such, it is the “predominant purpose” of the legislation that is relevant. If the doctrine treads incidentally or unintentionally, it should be upheld: “The question of invasion into the territory of another legislation is to be determined not by degree but by substance.” P.B. Sawant, J., has added in Vijay Kumar Sharma v. State of Karnataka that “[t]he legislation, to be on the same subject matter must further cover the entire field covered by the other.”

Conflict Between Entries Under the Seventh Schedule’s Concurrent list (list III)

54. Part of the Indian Constitution’s uniqueness comes from the fact that the Union and the State can both have jurisdiction over particular matters in the Seventh Schedule’s Concurrent List. When both Union and State choose to legislate over these entries of common jurisdiction, conflicts may arise. Courts resolve these conflicts by applying the doctrine of “repugnancy”, found in Article 254(1). Repugnancy arises where an apparent conflict between a Union law and a State law has the following three features: 1. The laws or provisions within the laws are fully and clearly inconsistent; 2. The inconsistency is irreconcilable; and 3. The inconsistency will bring the laws in direct conflict with each other such that one law cannot be obeyed without disobeying the other. As such, repugnancy arises where two laws give conflicting results when applied to an identical set of facts. In those cases, it is the Union law that applies. The State law is void to the extent of its repugnancy. As with other cases of apparent conflicts, however, everything must first be done to avoid repugnancy. Courts must attempt to reconcile the provisions harmoniously.


80 Shah Goverdhan, supra n. 74, at para. 7.


82 See, e.g., Kulwant Kaur and Ors. v. Gurdial Singh Mann (dead) by Lrs. and Ors. etc. AIR 2001 SC 1273 at para. 14.

83 S. Satyapal Reddy and Ors. v. Govt. of A.P. and Ors., 1994 (4) SCC 391 at para. 7.

84 Ibid.
55. A State Act cannot be said to be “implicitly” repugnant to a Union Act. For example, if Union and State acts create distinct and separate offences for the same behaviour, repugnancy will not apply: both acts will continue to apply. The Supreme Court has also stated, however, that for repugnancy to arise it is not necessary for one law to say “yes” and the other law to say “no”. The conflict can be more subtle, existing even where two laws say no, but in different ways. The case State of T.N. and Anr. Vs. Adhiyaman Educational & Research Institute and Ors., for example, found that there existed a conflict where the State imposed a minimum standard that was above the minimum standard imposed by the Union in institutions of higher learning.

56. Education cases have generally forced courts to find creative rules to determine the repugnancy of State legislation. Entry 25 of List III broadly covers “Education, including technical education, medical education and universities, subject to the provisions of Entries 63, 64, 65 and 66 of List I; vocational and technical training of labour.” Entry 66 of List I more specifically addresses the “Co-ordination and determination of standards in institutions for higher education or research and scientific and technical institutions.” Occasionally, therefore, a State will set standards as per Entry 25 of List III while the Union will set standards as per Entry 66 of List I. The Supreme Court devised a series of rules to determine where a State legislation is repugnant. First, the Court conclusively determined that the State could never impose lower standard than those standards imposed by the Union. The Court’s reasoning follows from the purpose of Entry 66, which is largely to allow the Union “to forge a uniform pattern for a concerted action according to a certain design, scheme or plan of development. It, therefore, includes action not only for removal of disparities in standards but also for preventing the occurrence of such disparities. It would, therefore, also include power to do all things which are necessary to prevent what would make “coordination” either impossible or difficult.” Second, as concerns higher standards set by the State, the Supreme Court broke down legislation into two categories. Higher standards would stand, the Supreme Court declared, wherever there existed more applicants than the available situation or seats: “When the State authority [sets higher standards in these cases], it does not encroach upon Entry 66 of the Union List or make a law which is repugnant to the Central law.” On the other hand, though, “when the situations/seats are available and the State authorities deny an applicant the same on the ground that the applicant is not

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87 Ibid, at para. 29.
qualified according to its standards or qualifications, as the case may be, although the applicant satisfies the standards or qualifications laid down by the Central law, they act unconstitutionally. So also when the State authorities derecognise or disaffiliate an institution for not satisfying the standards or requirement laid down by them, although it satisfied the norms and requirements laid down by the central authority, the State authorities act illegally.”

57. In light of its complicated rules for education, the Supreme Court has not been fully clear to what extent States can create different standards and offenses for the same matter. It seems, however, that the answer largely depends upon whether the Union expressly indicates its intention to legislate one consistent standard and offense. In fact, consistent with this interpretation, the Union can choose to “cover the field” of a particular Entry entirely. By indicating its intention to cover the entire field of an Entry, the Union thus prevents the State from legislating under that Entry. Any State legislation that relates in pith and substance to the Entry covered by the Union will be repugnant. But without a covered field, the State is free to legislate. This approach would be consistent with the Courts’ recent inclination to uphold State laws and areas of jurisdiction wherever possible.

58. The Supreme Court has also stated that the pith and substance doctrine applies to apparent conflicts between laws passed under different entries of concurrent jurisdiction, just as the pith and substance doctrine applies to conflicts between entries in different lists.88 Thus, Article 254(1) will only apply where the pith and substance of the two laws is identical. If they are not identical, and the State law only incidentally entrenches on the Entry according to which the Union has legislated, the State law will stand.

59. Courts will uphold repugnant State laws in one instance: where the law has received the assent of the President under Article 254(2). If the State law has received the assent of the President, it will overrule the provisions of the Union law against which it would otherwise have been repugnant. To cancel the Presidential assent, Parliament may at any time “make a law adding to, or amending, varying or repealing the law made by the State Legislature under the provision to Article 254.”89

60. If the government seeks the assent of the President for a particular reason, “the efficacy of the assent would be limited to that purpose and cannot be extended beyond it”90. However, if the government seeks the assent of the President in general terms, it will be effective for any purpose. As stated by K.

89 Ibid, at para. 15.
Ramaswamy J., “[o]n the other hand, the observation clearly indicates that if the assent is sought and given in general terms it should be effective for all purposes. In other words, this Court observed that the assent sought for and given by the President in general terms could be effective for all purposes unless specific assent is sought and given in which event it would be operative only to that limited extent.”

b. Taxation Entries

61. Taxation entries stand apart from other general entries in the Seventh Schedule, and courts have responded with particular rules for these entries. Article 265 of the Indian Constitution declares that “[n]o tax shall be levied or collected except by authority of law.” In conjunction with Article 245, it provides the basis for taxation by either the Union or the States. However, while federal countries like Canada allow both centre and provinces or states full discretion to create direct taxation on any matter linked to the jurisdiction, the Indian Constitution exhaustively enumerates and exclusively divides legislative powers of taxation between the Union and the States. In his Constitutional Law of India, H.M Seervai explains that: “The lists contained in the Schedule VII to the G.I. Act, 35, provided for distinct and separate fields of taxation…. List I and List II of Schedule VII thus avoid overlapping powers of taxation and proceed on the basis of allocating adequate sources of taxation for the federation and the provinces.”

The Concurrent List contains no taxation provisions, an objective certainly designed to minimize the possibility of taxation conflicts between Union and States. Again, Seervai observes that “it is not without significance that the concurrent legislative list contains no Entry relating to taxation but provides only for “fees” in respect of matters contained in the list but not including fees taken in any court.” In fact, the Supreme Court of India has determined that because of this fact, “in our Constitution, a conflict of taxing power of the Union and of the States cannot arise.” For this reason, it is equally implausible for a State tax validly imposed under a List II taxation Entry to conflict with a law imposed under a List III non-taxation Entry. Seervai concludes that the Constitutional setup means “that few problems of conflicting or competing taxing powers” would arise.

93 Ibid.
96 H.M. Seervai, supra n. 92.
Seervai is not completely correct. Because of the creation of distinct fields of taxation for Union and States, untangling what taxation rights belong to what jurisdiction in India can sometimes become more complex than in other federations. Union and States have clashed a few times over the power to impose certain taxes, with some issues ending up before the Courts since 1985 (which partially excuses Seervai, whose last edition of *Constitutional Law of India* dates from 1997). As with other legislative heads, the division of heads of taxation between Union and States appears in Article 246, by way of the Seventh Schedule’s Lists I and II.\(^7\)

List I of the seventh schedule assigns to the Union the following powers of taxation:

82. Taxes on income other than agricultural income.
83. Duties of customs including export duties.
84. Duties of excise on tobacco and other goods manufactured or produced in India except—
   (a) alcoholic liquors for human consumption;
   (b) opium, Indian hemp and other narcotic drugs and narcotics, but including medicinal and toilet preparations containing alcohol or any substance included in sub-paragraph (b) of this Entry.
85. Corporation tax
86. Taxes on the capital value of the assets, exclusive of agricultural land, of individuals and companies; taxes on the capital of companies.
87. Estate duty in respect of property other than agricultural land.
88. Duties in respect of succession to property other than agricultural land.
89. Terminal taxes on goods or passengers, carried by railway, sea or air; taxes on railway fares and freights.
90. Taxes other than stamp duties on transactions in stock exchanges and futures markets.
91. Rates of stamp duty in respect of bills of exchange, cheques, promissory notes, bills of lading, letters of credit, policies of insurance, transfer of shares, debentures, proxies and receipts.
92. Taxes on the sale or purchase of newspapers and on advertisements published therein.
92A. Taxes on the sale or purchase of goods other than newspapers, where such sale or purchase takes place in the course of inter-State trade or commerce.
92B. Taxes on the consignments of goods (whether the consignment is to the person making it or to any other person), where such consignment takes place in the course of inter-State trade or commerce.
92C. Taxes on services.
97. Any other matter not enumerated in List II or List III including any tax not mentioned in either of those Lists.

List II of Schedule 7 assigns to the states the following powers of taxation:

45. Land revenue, including the assessment and collection of revenue, the maintenance of land records, survey for revenue purposes and records of rights, and alienation of revenues.
46. Taxes on agricultural income.
47. Duties in respect of succession to agricultural land.
There are no heads of taxation under the Concurrent List. In *Synthetics & Chemicals v. State of U.P.*, the Supreme Court also confirmed that a tax had to be levied according to one of the taxation entries. It could not be levied under a general Entry.\(^98\) The residual power to impose taxation on matters not discussed in the other entries vests in the Union, as a result of Entry 97 of List I read in conjunction with Article 248(2).

62. Because powers of taxation belong exclusively either to the Union or to the States, courts tend to interpret taxation entries less broadly than they do other entries in the Seventh Schedule: “taxing entries must be construed with clarity and precision so as to maintain such exclusivity, and a construction of a taxation Entry which may lead to overlapping must be eschewed. If the taxing power is within a particular legislative field it would follow that other fields in the legislative lists must be construed to exclude this field so that there is no possibility of legislative trespass.”\(^99\) Taxation entries will still be

\(^{49}\) Taxes on lands and buildings.

\(^{50}\) Taxes on mineral rights subject to any limitations imposed by Parliament by law relating to mineral development.

\(^{51}\) Duties of excise on the following goods manufactured or produced in the State and countervailing duties at the same or lower rates on similar goods manufactured or produced elsewhere in India:—

(a) alcoholic liquors for human consumption;

(b) opium, Indian hemp and other narcotic drugs and narcotics; but not including medicinal and toilet preparations containing alcohol or any substance included in sub-paragraph (b) of this Entry.

\(^{52}\) Taxes on the Entry of goods into a local area for consumption, use or sale therein.

\(^{53}\) Taxes on the consumption or sale of electricity.

\(^{54}\) Taxes on the sale or purchase of goods other than newspapers, subject to the provisions of Entry 92A of List I.

\(^{55}\) Taxes on advertisements other than advertisements published in the newspapers and advertisements broadcast by radio or television.

\(^{56}\) Taxes on goods and passengers carried by road or on inland waterways.

\(^{57}\) Taxes on vehicles, whether mechanically propelled or not, suitable for use on roads, including tramcars subject to the provisions of Entry 35 of List III.

\(^{58}\) Taxes on animals and boats.

\(^{59}\) Tolls.

\(^{60}\) Taxes on professions, trades, callings and employments.

\(^{61}\) Capitation taxes.

\(^{62}\) Taxes on luxuries, including taxes on entertainments, amusements, betting and gambling.

\(^{63}\) Rates of stamp duty in respect of documents other than those specified in the provisions of List I with regard to rates of stamp duty.

\(^{98}\) *Synthetics & Chemicals Ltd*, supra n. 52.

interpreted liberally, but a court will not allow taxation statutes to intrude in Centre or State fields, or even go beyond the simple ordinary meaning of the words: “If in substance, the statute is not referable to a field given to the State, the Court will not by any principle of interpretation allow a statute not covered by it to intrude upon this field.”\[^{100}\] In *Godfrey Phillips India Ltd. v. State of U.P.*, for example, the Supreme Court of India determined that a State power to tax “luxuries, including taxes on entertainments, amusements, betting and gambling” (derived from Entry 62, List II) did not include the power to tax luxury goods.\[^{101}\] It only included the power to tax luxury activities. In *State of West Bengal v. Kesoram Industries Ltd. and Ors.*, the Supreme Court noted that a State tax on coal could not be justified by Entry 49 of List II, which only allowed the State to tax land or buildings. The tax on coal was “not directly upon the land but upon a part of land, which is mineral and, thus, out of the legislative competence of the State.”\[^{102}\]

63. To determine whether a tax is valid, Courts adopt a similar strategy to the one they use for legislation pertaining to other entries in the Seventh Schedule. However, while determining the validity of legislation pertaining to these other entries involves assessing the object of the legislation itself, determining the validity of taxation entries appears to be principally concerned with the object of the tax rather than the object of the legislation. Courts also focus on the object of the tax to the exclusion of the “incidence of tax” or the “machinery for the collection of the tax”:

“There is a distinction between the object of tax, the incidence of tax and the machinery for the collection of the tax. The distinction is important but is apt to be confused. Legislative competence is to be determined with reference to the object of the levy and not with reference to its incidence or machinery. There is a further distinction between the objects of taxation in our Constitutional scheme. The object of tax may be an Article or substance such as a tax on land and buildings under Entry 49 of List II, or a tax on animals and boats under Entry 58 List I or on a taxable event such as manufacture of goods under Entry 84 of List-I, import or export of goods under Entry 83 of List-I, Entry of goods under Entry 52 of List II or sale of goods under Entry 54 List II to name a few. Theoretically, of course, as we have held in *Godfrey Phillips India Ltd. v. State of U.P. and Ors. 2005 Scale Page 367*, ultimately even a tax on goods will be on the taxable event

\[^{100}\]Gujarat Ambuja Cements Ltd. and Anr. v. Union of India (UOI) and Anr. AIR 2005 SC 3020 at para. 21.
\[^{101}\]Godfrey Phillips, supra n. 99.
\[^{102}\]Kesoram, supra n. 28, para. 384.
of ownership or possession. We need not go into this question except to emphasise that, broadly speaking the subject matter of taxation under Entry 56 of List II are goods and passengers. The phrase “carried by roads or natural water ways” carves out the kind of goods or passengers which or who can be subjected to tax under the Entry.”

Once a court has agreed on the nature of a particular taxation Entry’s object, “all taxable events pertaining to the object are within that field of legislation unless the event is specifically provided for elsewhere under a different legislative head.”

64. In *State of Karnataka v. Drive-in-Enterprises*, for example, the State of Karnataka had levied an entertainment tax by passing the *Karnataka Cinemas (Regulation) Act, 1964* and related regulations for those persons who drove their car into a movie theatre to view the movie from their car. Drive-in-Enterprises challenged the Act on the grounds that the entertainment tax permitted by Entry 62 of List II could be levied only on human beings and not on an inanimate object such as a car. The Supreme Court rejected this challenge on the ground that the object of the tax was entertainment (and that the “pith and substance” of entertainment under Entry 62 of List II was broad enough to encompass the added entertainment that a person obtained by viewing a movie from their car). The manner in which the burden would fall on persons either with or without motor vehicles did not affect either the object of the tax. And cars were neither the object of taxation nor the taxable event; they were part of the incidence of the tax.

65. Despite the Constitution’s attempts to minimize conflict by exclusively dividing taxation powers between the Union and the States, there are instances where taxes either overlap or conflict. Through Entry 82 of List I, the Union is competent to tax “incomes” other than agricultural income. However, through Entry 60 of List II, it is State Legislatures that are competent to levy taxes on professions, trades, callings, and employments. These two types of taxes can overlap to an extent, because both can stem from the same source of income of a particular individual. Article 276 of the Constitution ensures that neither Union tax nor State tax will be deemed invalid. The Supreme Court of India has confirmed in *Karnataka Bank Ltd. v. State of A.P.* that apparently overlapping taxes in both of these entries are valid.

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103 Gujarat Ambuja Cements Ltd. and Anr. v. Union of India (UOI) and Anr. AIR 2005 SC 3020 at para. 28.
104 Godfrey Phillips, Supra n. 99, at para. 46.
105 AIR 2001 SC 1328
be construed in their widest amplitude. The field of legislation covered by the
Entry is not to be narrowed down in any way unless there is anything in the
Entry itself which defines the limits thereof.” In that sense, the Supreme
Court’s approach has maintained the full taxation power of Union and States,
even if it allows taxes to be levied on the same source of income. As with
conflicts between other entries, the Supreme Court since 1985 has sought to
minimize conflict between Union and States.

66. A number of other Constitutional provisions on taxation affect the relation-
ship between Union and the State. Articles 268-281, for example, distribute
taxation revenues between the Union and the States. Article 285 exempts
property of the Union from State taxation. Generally, however, these other
provisions have not given rise to judicial conflicts before the Supreme Court
of India, particularly since 1985. One exception concerns Article 286, which
provides that “[n]o law of a State shall impose, or authorise the imposition of,
a tax on the sale or purchase of goods where such sale or purchase takes place –
(a) outside the State; or (b) in the course of the import of the goods into, or
export of the goods out of, the territory of India.” This provision restricts the
taxation powers of States in certain instances. In State of A.P. v. National
Thermal Power Corpn. Ltd., the Supreme Court restricted the scope of Entry 53
of List II, which placed taxes on the consumption or sale of electricity as a
State head of legislation. The Supreme Court ruled that the sale of electricity
could not be separated from its consumption. Any out of State consump-
tion implied an out of State sale. Article 286 then applied to prevent the State
from taxing this out of State sale. In that sense, the Supreme Court’s interpre-
tation may have restricted the taxation power of the States, at least in the
field of electricity. But this decision is not enough to suggest that the Su-
preme Court generally has a restrictive approach toward the taxation power
of the States. It is more likely that the Supreme Court was merely stating that
“[n]o State legislation, nor any stipulation in any contract can fix the sites of
sale within the State or artificially define the completion of sale in such a way
as to convert an inter-State sale into an intra-State sale or create a territorial
nexus to tax an inter-State sale unless permitted by an appropriate Central
legislation.”

109 M.P. Singh, Constitution of India (Lucknow: Eastern Book Company, 2008) at 806-807
IV

Study of Major Legislative Developments in Respect of Centre-State Relations and Principle of Federalism in India

1. Introduction

67. In this part we try and highlight some major legislative developments having a bearing on Centre-State relations. Since a large number of legislations involving issues on Centre-State relations have been tested by the process of judicial review, the focus of this part is on major legislative developments which display the attitudes that governments have towards Centre-State relations and the principle of federalism. Though all legislation which have been enacted under overlapping entries in the Seventh Schedule involve issues of Centre-State relations, those issues get canvassed as issues of legislative competence and thus have been a subject matter of Part I of this paper.

68. Here we focus on four major areas which have witnessed significant legislative activity. These areas are national security, education, employment guarantee and environment. We also look at the effects that statues setting up regulatory authorities may have on Centre-State relations.

2. Legislations Regarding Public Order and National Security

a. The Terrorist and Disruptive Activities (Prevention) Act, 1985

69. The 1980s witnessed the rise of armed movements in various parts of India. The movements were particularly powerful in Punjab and Assam. Many perceived the situation as threatening the very basis of the federal Republic. One of the responses of the State to these movements, pursuant to the April 1985 bomb explosions in Delhi, was the enactment of the Terrorist and Disruptive Activities (Prevention) Act, 1985 (TADA). The Act was aimed to make provisions for the prevention of and the coping with terrorist and disruptive activities.

The TADA was introduced as a temporary measure to deal with the extraordinary situation created by the Khalistani secessionist violence. But the subsequent nine years saw it being replaced by the TADA and the same being extended four times and covering almost the whole of India before its Constitutional validity came to be questioned in Kartar Singh v. State of Punjab\textsuperscript{110}. In its actual operation, the ambit of the Act reached far beyond the

\textsuperscript{110} (1994) 3 SCC 569.
original context, to encompass all kinds of social tensions and political opposition. The ordinary criminal law was believed to be inadequate to deal with the ‘growing menace of terrorism’. Thus, a law authorizing the Government to take all steps expedient to deal with the situation was felt to be necessary by the State.

70. The implementation of the legislation saw rising opposition to it. This is evidenced by the more than four hundred writ petitions, Special Leave Petitions and appeals challenging the constitutionality of TADA which were pending before the Supreme Court. On 11 March 1994 the Supreme Court finally disposed this batch of petitions “without costs”. A Constitutional Bench comprising of Justices S.R. Pandian, M.M. Punchhi, K.Ramaswamy, S.C. Aggarwal and R.M. Sanai, upheld the constitutional validity of TADA. The majority judgment was delivered by S.R.Pandian, and two minority judgements were delivered by R.M. Sahai and K. Ramaswamy.

Legislative Competence

71. On legislative competence it was argued that the Act fell within the purview of maintenance of ‘public order’- a subject matter under the State List and thus Parliament did not have the competence to enact the legislation. The Court however held that the Parliament had the competence to enact the legislation as it fell under Entry of List I which deals with ‘Defence of India’. The Court justified this on two arguments:

a. There was a clear distinction between ‘public order’ and ‘law and order’ on the one hand and ‘Defence of India’ on the other. The former two referred to problems of lesser magnitude which were restricted to the territorial boundaries of the State concerned.111 The latter applied to situations where there were threats of a greater magnitude.

“Activities of a more serious nature which threaten the security and integrity of the country as a whole would not be within the legislative field assigned to the States under Entry 1 of the State List but would fall within the ambit of Entry 1 of the Union List relating to defence of India and in any event under the residuary power conferred on Parliament under Article 248 read with Entry 97 of the Union List. The petitioners can succeed in their challenge to the validity of the Act with regard to the legislative competence of Parliament, only if it can be said that the Act deals with activities relating to public order which are confined to the territories of a particular State.”112

111 Ibid at para. 65 and 66.
112 Ibid at para. 66.
b. The Court raised the spectre of threats posed by anti-national and external forces to assert that the pith and substance of TADA concerned something of much graver consequence than mere threat to public order. It was the sovereignty and security of the country which was at stake. So the Act was pronounced to fall in the domain of ‘Defence of India’, a Union subject.

Impact on Centre-State Relations

72. Though the TADA was claimed to be an enactment for a specific purpose, the Union Government gave it five new leases of life. This has resulted in a continuous interference of the Union Government in affairs within the territorial boundaries of the State.

73. The TADA tremendously increased the power of the Police, which is under the control of the State Government. This however, did not mean that the State Government was in a position to decide on the manner in which it was to deal with cases to which the act applied. Provisions of the Act made it clear that the Central Government would be the ultimate determiner of the manner in which the Act was to be implemented.

74. Section 7 of the Act empowered the Central Government to confer on any of its officers, powers exercisable by a police officer under the code, in particular the powers of arrest, investigation and prosecution of persons before any court. All officers of the Police and Government were required to assist the officer of the Central Government in the execution of the provisions of the Act and any rule made thereunder.

75. Section 9 of the Act empowered the Central and State Governments to set up designated courts under the Act. However, in case a designated court was set up by both governments in the same area, then the Court set up by the Central Government was to have jurisdiction to the exclusion of the Court constituted by the State.

76. These provisions thus clearly left it to the option of the Central Government to take over matters under the Act into its own hands to the exclusion of the State Government.

77. The TADA has been continuously criticised by civil society groups to be a draconian legislation. The reasons for such criticism have been that its provi-
sions violate the principles of natural justice, criminal law and the law of
evidence. The state has also been accused of misusing the Act against civil
rights activists and persons who hold an opinion of Indian federalism which
differs from that of the Indian state.\textsuperscript{113}

b. \textbf{The Prevention of Terrorism Act, 2002}

78. The controversial Prevention of Terrorism Act, 2002 was passed in the wake
of incidents such as the terrorist strikes on the World Trade Centre on Sep-
tember 11\textsuperscript{th}, 2001 and the attack on the Indian Parliament on December 13\textsuperscript{th},
2001 to curb the menace of terrorism. Civil rights groups were critical of the
legislation which they believed posed a grave threat to individual freedom
and liberty. The political class was intensely divided over the provisions of
the Bill, so much so that it required a rare joint sitting of both Houses of
Parliament on the 26\textsuperscript{th} of March, 2002 to have it enacted.

\textbf{Legislative Competence}

79. The Constitutional validity of the Act was challenged in \textit{Peoples Union for Civil
Liberties and Anr. v. Union of India.}\textsuperscript{114} Besides contending that specific provi-
sions of the Act were violative of the various fundamental rights guaranteed
in Part III of the Constitution, the petitioners argued that Parliament lacked
the legislative competence to enact the law in the first place. According to the
petitioners, the provisions of POTA, in pith and substance fell under Entry 1
of the State List dealing with “public order”. They submitted that terrorist
activities were confined to States and hence, the States had the competence
to come up with a law in this regard. The Union of India on the other hand,
argued that acts of terrorism, which were aimed at weakening the sovereignty
and integrity of the country could not be equated with mere breaches of law
and order and disturbances of public order and public safety. The legislative
competence of the State to enact laws for its security could not denude the
Parliament of its competence under List I to enact laws to safeguard national
security and sovereignty of India by preventing and punishing terrorist acts.\textsuperscript{115}

\textsuperscript{113} ‘TADA Judgment, A Critique’, \textit{People’s Union for Democratic Rights}, available at \url{http://cssh.unipune.ernet.in/HumanRights/01%20STATE%20DEMOCRACY%20AND%20LAW/21%20PUDR%20TADA%20Judgment%20-%20Critique%20Delhi%20May%20201994.pdf}, (Last
visited on 15\textsuperscript{th} December, 2009.)

\textsuperscript{114} (2004) 9 SCC 580.

\textsuperscript{115} Ibid, at para. 2-3.
80. The two Judge Bench comprising Justices S. Rajendra Babu and G.P. Mathur upheld the constitutional validity of the Act. It expressed its agreement with all the contentions of the Union of India in defence of the law and found little substance in the petitioner’s fears regarding violations of individual freedom and liberty. Studying the judgment, V. Venkatesan noted:

“The Bench ...made it clear that it could not examine the “need” for POTA.” It is a matter of policy. Once a piece of legislation is passed, the government has an obligation to exercise all available options to prevent terrorism within the bounds of the Constitution,” it said. The Bench found that Parliament concluded that the existing laws were not capable of tackling terrorism, and that terrorism is not a usual law and order problem. It referred to the statement of Home Minister L.K. Advani, made while piloting the Bill, and underlined his claim that cross-border state-sponsored terrorism was the reason for the enactment of POTA.

Advani’s claim could perhaps indicate the government’s intention in enacting the law. However, there could be serious disagreement over whether Parliament agreed collectively with this perception. Having failed to secure the passage of the law in the Rajya Sabha, the government used the provision enabling the holding of a joint session of Parliament to pass the Bill. A bitter debate over the substantial provisions of the law preceded its passage. Yet, law-makers had no clue about how the existing laws were not capable of tackling terrorism. It is curious that the Bench ignored this contextual backdrop to the enactment of POTA, although it dealt at length with the modern aspects of terrorism and its growing challenge to the civilised world, while justifying the legislative competence of Parliament to enact such a law.16

81. In upholding the constitutional validity of the POTA, the Court applied the same logic which was used to uphold the TADA. In justifying the need for such a legislation the Court referred to the prevailing circumstances of the country in the following terms:

“The terrorist threat that we are facing is now on an unprecedented global scale. Terrorism has become a global threat with global effects.

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It has become a challenge to the whole community of civilized nations. Terrorist activities in one country may take on a transnational character, carrying out attacks across one border, receiving funding from private parties or a government across another, and procuring arms from multiple sources. Parliament has passed POTA by taking all these aspects into account."

The Court held that terrorists’ acts could not be equated too law and order problems:

“Terrorist acts are meant to destabilize the nation by challenging its sovereignty and integrity, to raze the Constitutional principles that we hold dear, to create a psyche of fear and anachronism among common people, to tear apart the secular fabric, to overthrow democratically elected government, to promote prejudice and bigotry, to demoralize the security forces, to thwart the economic progress and development and so on. This cannot be equated with a usual law and order problem within a State.”

82. Referring to the speech of the Home Minister in the joint Parliamentary session the Court came to the conclusion that “the Parliament has explored the possibility of employing the existing laws to tackle terrorism and arrived at the conclusion that the existing laws are not capable. It is also clear to Parliament that terrorism is not a usual law and order problem.

83. The Court went on to hold that the Entry “Public order” in the State List empowered the State to enact legislation relating to the public order and security of that particular State. Therefore, no matter how widely the Entry was read, it could not bring within its ambit the present day problem of terrorism. On this logic, the Court held that one could not rely on the decisions in Romesh Thaper, Dr. Ram Manohar Lohia and Madhu Limaye, since the Entry “Public Order” or any other Entries in List II do not cover the situation dealt within POTA.

84. The POTA was passed in an extraordinary joint session of the Parliament. This was necessitated by the fact that the Rajya Sabha had rejected the bill.
The usual procedure in such a situation is to refer the Bill to a select committee of the Parliament. Instead the government bypassed this procedure and passed the law in a joint session of the Parliament. This reflects a subversion of the procedure which safeguards federalism.120 The decisions of the Court pursuant to the enactment of the POTA also reflect centralising tendencies. For example, in the case of withdrawal of prosecution under the POTA by the Uttar Pradesh Government, the Supreme Court held that the trial court could not drop charges under POTA at the behest of the State Government, since the State Government could not take decisions under a central law.121

c. The National Investigation Agency Act, 2009

85. The need for a National Investigation Agency (NIA) has been highlighted time and again by a number of government institutions, agencies and independent committees including National Human Rights Commission, the Soli Sorabjee Committee, the Bureau of Police Research & Development, (BPR&D) and the Second Administrative Reforms Commission.122

86. The creation of such an agency has been justified on the ground that since “terrorism” today has national ramifications, there is a need for an agency which is not constrained by State boundaries and laws. The problem being one at a national level, the solution too must be at the same level.

87. On the necessity of such an agency, the Malimath Committee on the Reforms of the Criminal Justice System remarked:

“Time has come when the country has to give deep thought for a system of Federal Law and Federal Investigating Agency with an all-India charter. It would have within its ambit crimes that affect national security and activities aimed at destabilising the country politically and economically. The creation of the Federal Agency would not preclude the State Enforcement Agencies from taking cognisance of such crimes. The State Enforcement Agencies and the Federal Agency can have concurrent jurisdiction. However, if the Federal Agency takes up the case for investigation, the state agencies’ role in the investigation would automatically abate. The state agencies may also refer complicated cases to the proposed Federal Agency.”123

120 Ujjwal Kumar Singh, POTA and Federalism, Economic and Political Weekly, Vol XXXIX No. 18 May 1 2004, at 1794.
121 Ibid, at 1795.
123 (See COMMITTEE ON REFORMS OF CRIMINAL JUSTICE SYSTEM STUDY, VOL. I, MINISTRY OF HOME AFFAIRS, GOVERNMENT OF INDIA, MARCH 2003, PARA 18.12)
88. The Committee recommended that the Federal Agency may have concurrent jurisdiction over the following categories of crimes:

i. Terrorist activities/ war against the State

ii. Arms and drug trafficking

iii. Hijacking

iv. Money laundering

v. Crimes related to counterfeit currency

vi. Espionage

vii. Crimes targeting the national infrastructure.

Summary of the legislation

89. According to the Act, investigation of Scheduled offences is contingent upon the State Government perceiving that such a crime has been committed and sending a report to the Centre in this regard. Upon receipt of such a report, the Centre will decide within fifteen days whether the said offence is scheduled or not. In special circumstances, if the Centre is of the view that a Scheduled Offence has been committed, then it may suo moto direct the NIA to investigate such an offence. Prosecution of Scheduled Offences would be conducted by constituting one or more Special Courts, which will be presided over by a judge appointed by the Central Government on the recommendation of the Chief Justice of the High Court.

1. CONSTITUTIONAL VALIDITY OF THE NIA

90. The Constitutional validity of the NIA Act is ambiguous. Policing and public order being State subjects, the legislation might be perceived as encroaching upon legislative fields reserved for the States. This view has been endorsed by many of the earlier committees who have examined the issue. Many of them have pointed out that the “it should be clearly understood that the aim of creating such an agency, by whatever name called, cannot be to usurp the powers of the State, but on the other hand, it should be an agency meant to assist them in the nation’s fight against terrorism and inter-State or trans-national organized crime which jeopardise national security.”

91. Despite the fact of “policing” and “law and order” being State subjects, the following arguments have been advanced to imagine the possibility for the Centre to enact a law providing for the NIA:

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124 Supra n. 122.
125 Ibid.
a. Entry 93 of List I, provides the Centre the power to legislate on “offences against laws with respect to any of the matters in this List”. Thus the Parliament could pass a law providing for the NIA to deal with specific offences. The argument against seems to be that such a law provides for dealing with specific offences and not to establish a new agency. The language of the Entry seems to suggest that the power is to create offences and not to establish agencies. It has been held earlier that the Union legislature would have exclusive power to create offences with regard to matters in List I.  

b. Entry 1 of List I “the defence of India”, read in conjunction with Article 355 of the Constitution is sufficient to allow the Centre to provide for the NIA by way of legislation.

Apart from the means of legislation, the Law Ministry has opined that in the absence of a Constitutional Amendment, the creation of a national investigation agency with enforcement powers must rely on recourse to Article 249 or 252 of the Constitution. This would mean that a national policing agency would be able to investigate a cross-jurisdictional crime only at the request or with the consent of the State concerned. The NIA however can assume jurisdiction over a Scheduled Offence _suo motu._

**Impact on Centre-State Relations**

92. The concerns about the NIA have not only been with regard to the competence of the Parliament, but also with regard to the broad powers conferred on the Central Government by use of open ended language in the legislation. For example, “Section 6(3) of the Act states that the Central Government shall determine … within 15 days … whether the offence is a Scheduled Offence or not and also whether, having regard to the gravity of the offence and other relevant factors, it is a fit case to be investigated by the Agency.” The open endedness of phrases such as “other relevant factors” (without explaining what these factors might be) allows in the possibility of political expediency playing a role in the Centre’s determination of whether to direct the Agency to investigate or not.” Section 7 of the Act also permits the consideration of “other relevant factors” when deciding whether to collaborate or transfer an investigation to the State. The use of such words gives

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127 Supra n. 122.
128 Ibid.
129 Ibid.
130 Ibid.
131 Ibid.
an impression that the option of having concurrent jurisdiction and collaborating with the States is contingent on the wish of the Central Government. It also creates such a situation in the context of determining scheduled offences. These situations seem to create a situation where the powers of the Central Government can make serious inroads into the fields of activity reserved for the State Government. Though it might be desirable to have a central agency to have efficient solutions to security problems, the discretionary powers conferred on the Central Government have caused concerns in many sectors about the power relations between the Centre and the States.

3. **Legislations on education.**

93. The establishment of the Central Advisory Board of Education (CABE) in 1920 by the colonial government marked the beginning of centralised coordination of education in India. It was dissolved in the year 1923 but was revived again in 1935. Though most matters related to education are covered by government policies, matters related to higher education are also governed by legislations. Apart from University Grants Commission, the Government of India implements its policies on education through various councils like the National Council of Educational Research and Training, Indian Council of Social Science Research, Indian Council of Agricultural Research etc.

94. Post 1984, there has been at least two major legislative developments in the field of education with a bearing on Centre-State relations. These are the enactment of the All India Council for Technical Education Act, 1987 and the National Council for Teacher Education Act, 1993. Both legislations have invited the attention of the Courts on more than one occasion on issues related to legislative competence. In this section we look at the impact that these legislation have on Centre-State relations.

95. Entry 25 of List III and Entry 66 of List I deal with education in general terms. Entries 63-65 in List I deal with matters pertaining to particular educational institutions.

Entry 66 of List I, of the Constitution reads as follows:

66. Co-ordination and determination of standards in institutions for higher education or research and scientific and technical institutions.

Entry 25 of List III reads as follows:

25. Education, including technical education, medical education and universities,
subject to the provisions of Entries 63, 64, 65 and 66 of List 1; vocational and technical training of labour.

96. Entry 25 clearly gives pre-dominance to the field assigned to the Union for matters relating to education. Like in the case of all other entries where the Union’s field receives priority, it is possible to measure the deference showed to States by examining the extent to which the field has been occupied by the Union. In what follows, we examine the provisions of the legislation along with judicial decisions interpreting them, in order to measure the extent of the field covered by the Centre and its possible implications.

a. The All India Council for Technical Education Act, 1987

97. The Act establishes the ‘All India Council for Technical Education’ (AICTE). The preamble to the Act states that the AICTE is established for the following reasons:

♦ proper planning and co-ordinated development of the technical education system throughout the country,
♦ the promotion of qualitative improvement of such education in relation to planned quantitative growth; and
♦ regulation and proper maintenance of norms and standards in the technical education system and for matters connected therewith.

These objectives display a two-fold concern. The first is with regard to qualitative improvement of technical education. The second is regarding the coordinated development of the technical education system throughout the country. These concerns are to be achieved by proper planning and maintenance of standards.

Issues with bearings on Centre-State relations:

1. Inclusion of different regions in decision making:

143. Section 10 of the Act states that the Council can take all such steps as it may think fit for ensuring co-ordinated and integrated development of technical education and maintenance of standards. The Council may, amongst other things:

♦ Coordinate the development of technical education in the country at all levels;
♦ Evolve suitable performance appraisal systems for technical institutions and universities imparting technical education, incorporating norms and mechanisms for enforcing accountability;

♦ Lay down norms and standards for courses, curricula, physical and instructional facilities, staff pattern, staff qualifications, quality instruction, assessment and examinations;

♦ Grant approvals for starting new technical institutions and for introduction of new course or programmes in consultation with the agencies concerned.

♦ Set up a National Board of Accreditation (NBA) to periodically conduct evaluation of technical institutions and programmes on the basis of guidelines, standards and norms, specified by it, and to make recommendations regarding recognition and derecognition of the institution or the programme.

144. It is arguable that achieving a high and common standard of norms for technical education is important for people to work together in an economy and society. Thus the want for coordination justifies constituting a body which would evolve such norms and administer them. At the same time it is important to take into account the fact that norms are not set at a standard which makes them unattainable for some. The ability to satisfy standards is to a great extent dependent on the socio-economic circumstances of persons and historical realities through which communities have lived. These arguments justify the claims of States to participate in norm making processes.132 Certain States may also feel that they need people with expertise in areas which may not be relevant for a majority of the States or which may not find mention in the policies of the Centre. Such claims may not require an exclusive field of legislation for the State as the Central legislation may itself provide for such concerns.

145. The AICTE Act contains some provisions which may address these concerns. It provides for setting up regional committees and having the chairmen of those committees as members of its executive council. The rules constituting these committees and setting out their powers and functions are to be made by the AICTE itself. In terms of numbers, the executive council finds a large number of persons appointed by the Central Government apart from representatives from educational institutions.133 The representatives of the Central

132 The need for having standards which are uniform but which are sensitive to the historical and socio-economic realities of different communities has been highlighted by the Supreme Court of India in State of T.N. and Anr. v. Adhiyaman Educational & Research Institute and Ors, supra n. 86.

133 All India Council of Technical Education Act, 1987, S. 12.
Government clearly outnumber those of the regional committee. The emphasis on centralized coordination is thus clear in the manner in which the council is constituted.

146. The Act is a legislation which deals with technical education. If technical education can be justifiably called a specialized field demanding inputs by experts, then the Act would not raise questions with bearing on Centre-State relations. This is so because irrespective of the States one was concerned with, the issues with regard to technical institutions would be the same. However, since ‘technical education’ covers a wide range of fields without any clear criteria delineating its area of operation, there is a potential for Centre-State issues to arise. State Governments which wish to promote a particular kind of technical education which does not find favour in the Central Government policy, would have to seek approval from the AICTE and comply by its norms. Such situations may cause tensions to arise between the State Government and the Centre. However, the probability of such tensions arising would be dependent on the capacity of the AICTE norms to accommodate different requirements without compromising on minimum standards. Minimum standards in turn may also prove to be a source of tensions if they are pitched at a level unattainable for many States due to historical reasons and lack of resources. Thus, it is necessary that structural changes are put in place to make the voices of States more real in decision making by the AICTE. In the alternative the same could be achieved by developing healthy practices of widespread consultations with various voices from the States before the AICTE formulates its standards.

2. **Ultimate control vests with the Central Government**

102. The AICTE Act makes it clear that the ultimate powers of policy and decision making lie with the Central Government. The AICTE is bound by directions of the Central Government on questions of policy. Whether the particular question is a question of policy or not is to be made by the Central Government. These provisions, read together, mean that the Central Government can bind the AICTE on any matter that it thinks is one of policy. It remains to be seen how a court of law would define matters of policy with regard to technical education. In the absence of any such distinction, the Act confers an unqualified power on the Central Government to bind the AICTE.

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134 Ibid, S. 20 (1).
135 Ibid, S. 20 (2).
In the face of such control, coupled with the provisions on composition of the Council, it becomes clear that the degree of independence of the council depends on the way the Central Government chooses to exercise its vast powers under the Act.

103. The Act also empowers the Central Government to supersede the AICTE.\textsuperscript{136} Supersession would amount to \textit{inter alia}:

\begin{itemize}
  \item vacation of offices by all members
  \item all powers of the Council being performed by persons directed to do so by the Central Government
  \item all the property of the council vesting in the Central Government
\end{itemize}

After the period of supersession expires, the Central Government may either extend the period or reconstitute the council as per Section 3.

104. These provisions clearly provide the occasion for the Central Government to exercise complete control over the AICTE.

3. Issues of Legislative Competence

105. Being enacted under Entry 66, List I and Entry 25, List III, a State cannot make a law on any matter which is inconsistent with the AICTE Act.

106. In \textit{State of T.N. and Anr. v. Adhiyaman Educational & Research Institute and Ors.},\textsuperscript{137} the question involved was whether after the coming into force of the AICTE Act the State Government had power to grant and withdraw permission to start a technical institution as defined in the AICTE Act. It was held that the AICTE Act was referable to Entry 66 of List I. After the Constitutional Amendment (42 Amendment Act, 1976) Entry 25 of List-III in the Concurrent List read: “Education, included technical education, medical institution and Universities, subject to the provisions of Entries 63, 64, 65 & 66 of List-I; vocational and technical training of labour”. Thus, the State law under Entry 25 of List-III would be repugnant to any law made by the Parliament under Entry 66 of List I, to the extent of inconsistency.

107. This decision clearly reserves vast powers of decision making for the AICTE. This effectively means that the State Governments have no power to legislate on substantial matters regarding technical education. The decision making powers now lie with the AICTE which is a body with a dominant presence of

\textsuperscript{136} Ibid, S. 21.

\textsuperscript{137} Supra n. 86.
representatives from the Central Government. This is mitigated to a certain extent by the presence of members from technical institutions. In spite of this mitigating factor, it is clear that the State Governments have no role to play in the important matters dealt with by the AICTE. The Supreme Court was sensitive to this point and thus was careful in pointing out that the powers of the council were justified by the need for coordinated and planned development of technical education. The council therefore had a dual task of preventing lopsided development of technical education in the country and ensuring that the norms and standards it designed were suitable to people all across the country. The words of the Court make this concern evident:

"...The norms and standards have, therefore, to be reasonable and ideal and at the same time, adaptable, attainable and maintainable by institutions throughout the country to ensure both quantitative and qualitative growth of the technically qualified personnel to meet the needs of the country. Since the standards have to be laid down on a national level, they have necessarily to be uniform throughout the country without which the coordinated and integrated development of the technical education all over the country will not be possible which will defeat one of the main objects of the statute.... Unnecessarily high norm or standards... may not only deprive a vast majority of the people of the benefit of the education and the qualification, but would also result in concentrating technical education in the hands of the affluent and elite few and in depriving the country of a large number of otherwise deserving technical personnel.."\(^{138}\)

The Court also held that Entry 66, should not be interpreted in a restricted manner and the power to legislate on a subject should normally be held to extend to all ancillary or subsidiary matters which can fairly and reasonably be said to be comprehended in that subject. The expression “co-ordination” used in Entry 66 does not merely mean evaluation. According to the Court:

"It means harmonization with a view to forge a uniform pattern for a concerted action according to a certain design, scheme or plan of development. It, therefore, includes action not only for removal of disparities in standards but also for preventing the occurrence of such disparities. It would, therefore, also include power to do all things which are necessary to prevent what would make “coordination” either im-

\(^{138}\)Adhiyaman Educational & Research Institute, supra n. 86, at para 24.
possible or difficult. This power is absolute and unconditional and in the absence of any valid compelling reasons, it must be given its full effect according to its plain and express intention."

108. The decision in *Adhiyaman Educational* suggests that the Court's interpretation has substantially reduced the space available to State Legislatures under Entry 25. This view would have been justified till the decision in *Govt. of A.P. and Anr. v. J.B. Educational Society and Anr.*. In this decision the Court held that Section 20(3) of the A.P. Education Act, 1982 was not inconsistent with Section 10 of the AICTE Act. The State legislation required that to establish an educational institution, any agency or authority had to seek permission from the competent authority under the Act. Responsibilities of the competent authority included the determination of educational requirements of an area. The J.B. Educational society was refused permission by the competent authority on the grounds that the area in question did not require the establishment of engineering colleges which the society proposed to establish. The society challenged the refusal of permission and also the Constitutional validity of the Section 20 (3) of the State Act.

109. The Court held that the State Government was well within its powers to assess the educational requirements of areas within its jurisdiction and Entry 25 of the Concurrent List provides competence to the State Legislature to make laws regarding education, including technical education. Though Section 10(s) of the AICTE Act provided for surveys to be conducted by the AICTE, such surveys were for the purposes of determining the standards of technical education and not the educational needs of an area. Thus there was no conflict between the provisions of the two legislations.

110. In *J.B., Educational Society* the Court has supplied an interpretation which preserves an area of operation for the legislative power of States within the field of Entry 25. This is in spite of the ‘subject to’ clause in Entry 25 List II and the mandate for wide interpretation of Entry 66 of List I, both of which can serve as invitations to allocate a larger playing field for the Central Legislature.

4. The question of approvals

111. Under Section 10(k) of the AICTE Act, the Council has the power to grant approval for starting technical institutions. The Supreme Court has held that a law requiring the approval of a State Government to start such an institution

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139 Ibid, at para 43.
will be repugnant to the AICTE Act. The Central Act occupies the field relating to grant of approvals, and the provisions of the Central Law alone should be complied with.\(^1\) This position has become qualified after the decision in *JB Educational Society* as the inquiry now is about the purposes for which approvals are being granted. The State Legislature would be competent to make law which concerns grant of permissions on the basis of educational requirements of an area.

112. The decision in *JB Educational Society* seems to be an exception since, in all other cases the Court has held that the State Government has no role to play in granting approvals in matters relating to technical education. In *All India Council for Technical Education v. Surinder Kumar Dhawan and Ors* \(^2\) the Court held that it is the function of the AICTE to consider and grant approval for introduction of any new course or programme in consultation with the agencies concerned. It was held that the decision whether a bridge course should be permitted as a programme for enabling diploma holders to secure engineering degree, and if permitted, the norms and standards regarding Entry qualification, content of course instructions and manner of assessing the performance by examinations, are all decisions in academic matters of technical nature.

113. The Court went on to hold that the decision of the AICTE not to permit bridge courses for diploma holders and its decision not to permit those who have passed 10+1 examinations (instead of 10+2 examination) to take the bridge course, relate to technical education policy which falls within the council’s exclusive jurisdiction.

114. In *Jaya Gokul Educational Trust v. The Commissioner & Secretary to Government Higher Education Department, Thiruvanantapuram, Kerala State & Another* \(^3\), it was held that there was no statutory requirement for obtaining the approval of the State Government and even if there was one, it would have been repugnant to the AICTE Act. The AICTE Act and in particular, Section 10(k) occupied the field relating the ‘grant of approvals’ for establishing technical institutions and the provisions of the AICTE Act alone are to be complied with:

“As far as the provisions of the Mahatma Gandhi University Act or its statutes were concerned and in particular statute 9(7), they merely required the University to obtain the ‘views’ of the State Government.

\(^1\) Unnikrishnan J.P. v. State of Andhra Pradesh, AIR 1993 SC 2178; Shah Goverdhan, supra n. 74.

\(^2\) JT 2009 (5) SC 216.

\(^3\) (2000) 5 SCC 231.
That could not be characterized as required the “approval” of the State Government. If, indeed, the University statute could be so interpreted, such a provision requiring approval of the State Government would be repugnant to the provisions of Section 10(K) of the AICTE Act, 1987 and would again be void.”

The decisions of the Court make it clear that all matter pertaining to technical education fall within the exclusive jurisdiction of the AICTE. The decision in *JB Educational Society* preserves some space for the State Governments to have a say, but the intention of the legislature to bring matters of technical education under central coordination has been affirmed by the Courts. At present the structure of the legislation and the judgments of the Court make the chance of including voices of the States completely dependent on the discretion of the AICTE which is clearly dominated by the representatives of the Central Government.

**b. The National Council for Teacher Education Act, 1993**

115. The National Council for Teacher Education Act, 1993 (NCTE Act) was enacted by Parliament and came into force from July 1, 1995.

116. The NCTE is a statutory body set up under the Act. Its objectives are to facilitate planned and coordinated development of teacher’s education and regulation and proper maintenance of norms and standards in the teacher education system. The mandate given to the NCTE is very broad and covers the whole gamut of teacher education programs including research and training to teach at pre-primary, primary, secondary and senior secondary stages in schools, and non-formal education, part-time education, adult education and distance (correspondence) education courses.

117. NCTE has its headquarters at New Delhi headed by a Chairperson. It has four Regional Committees at Bangalore, Bhopal, Bhubaneswar and Jaipur each bring headed by a Regional Director.

118. Chapter III of the Act deals with the functions of the Council. The Council, under Section 12 is responsible for the following activities and functions:

i. to coordinate and monitor teacher education and its development in the country;

ii. lay down guidelines in respect of minimum qualifications for a person to be employed as a teacher;
iii. lay down norms for any specified category of courses or trainings in teacher education;

iv. lay down guidelines for compliance by recognized institutions for starting new courses or training;

v. lay down standards in respect of examinations, leading to teacher education qualifications; and

vi. examine and review periodically the implementation of the norms, guidelines and standards laid down by the Council.

119. Section 14 deals with recognition of institutions offering courses or training in teacher education. It makes it mandatory for every institution offering a course or training in teacher education to make an application for recognition under the NCTE Act. Refusal of recognition by the NCTE would require the institutions to discontinue the course or training. Permission is also to be sought for any new course that a recognised institution seeks to start.\(^\text{144}\)

120. The Act also empowers the NCTE to withdraw recognition of institutions which contravene the provisions of the Act or the rules and regulations made under it.\(^\text{145}\) The NCTE thus, has vast powers with regard to teachers’ education. No institution intending to offer training to teachers can do so without its approval.

121. Like the AICTE Act, the powers of the NCTE are to be exercised by a council, the composition of which is dominated by persons who are representatives of the Central Government.\(^\text{146}\) Thus the implications of such a composition which apply to AICTE, apply to the NCTE too. Other provisions of the NCTE Act are also \textit{pari materia} to the AICTE Act. The conditions for exercise of the power of supersession and the binding nature of the Central Governments directions on policy matters are the same in both Acts.\(^\text{147}\) Thus, the possibility of complete control by the Central Government at its

Scope of the Legislation

122. In \textit{Basic Education Board, U.P. v. Upendra Rai and Ors.}\(^\text{148}\) Supreme Court clarified the scope of the legislation by interpreting the term ‘institution’ in S. 2(c) of

\(^{144}\) NCTE Act, S. 15

\(^{145}\) Ibid, S. 17.

\(^{146}\) S. 3 of the Act provides for the composition of the council. The scheme of this provision is similar to the corresponding section in the AICTE Act.

\(^{147}\) NCTE Act, Ss. 29 and 30.

\(^{148}\) (2008) 3SCC 432.
the Act. The term was held to mean an institution which offers courses or training in teacher education. Thus the Act does not deal with ordinary educational institutions like primary schools, high schools, intermediate college or university. It is only teachers’ training institutions which have to seek grant of recognition or continuation of recognition from the Regional Committee. The ordinary educational institutions do not have to seek any such recognition or continuation under the NCTE Act.

Legislative Competence

123. The Constitutionality of the NCTE Act and section 17 (4) in particular was questioned in Union of India (UOI) and Ors. v. Shab Goverdhan L. Kabra Teachers College\(^ {149}\). The challenge was on the ground of legislative competence. It was contended that the Act was not a law dealing with coordinated development of education system within Entry 66 of the List I of the Seventh Schedule. Rather it is a law dealing with the service conditions of an employee under the State Government. The Supreme Court applied the rule of pith and substance and held that the NCTE Act and more particularly Section 17(4) deals with coordination and determination of standards in institutions for higher education within the meaning of Entry 66 of List I of the Seventh Schedule. The Court held that the object behind the Act was that the standards are not lowered at the hands of the particular State or States to the detriment of national progress and the power of the State Legislature must be so exercised as not to directly encroach upon power of Union under Entry 66.

124. In State of Maharashtra Vs. Sant Dnyaneshwar Shikshan Shashtra Mahavidyalaya and Ors.\(^ {150}\), the Supreme Court held that the State Government had no power to refuse permissions for establishing new B. Ed. colleges on the basis of local considerations. The Court was of the opinion that the Central Government had completely occupied the field by promulgation of the NCTE Act and thus the State Government had no role to play in such matter.

125. It is interesting to note that the State Government had contended that it was well within its power to consider whether the areas within its jurisdiction required the setting of more B. Ed. colleges. This was a matter of policy where the educational requirements of the State were to be kept in mind. The Court however expressly rejected this argument. This argument however, was accepted by the Court in the case of JB Educational Society in the context of the

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\(^{149}\) Supra n. 74.

AICTE Act. It is not the case that in Sant Dnyaneshwar the Court made a distinction between the NCTE and the AICTE Acts. Rather it relied on cases pertaining to the AICTE Act to support its reasoning and decision on the ground that the provisions of the two legislations were almost similar. It thus remains to be seen how the Court resolves the positions in JB Educational Society and Sant Dnyaneshwar once the conflict is brought to its attention.

c. The Right of to Free and Compulsory Education Act, 2009

126. The legislation enacted in August 2009, aims to provide free and compulsory education to children between 6-14 years of age. The legislation lays out the roles to played by the Union, State, and local governments. Chapter III of the Act lays down the duties of each tier of government. The pattern of this layout is similar to that of the division of duties provided under the National Rural Employment Guarantee Act, 2005 which is examined in the next section.

127. The legislation states that the nature of the duties and responsibilities of the Central and State Governments is a concurrent one. With regard to establishment of education institutions, the three tiers of government are to be responsible in their respective jurisdictions.\footnote{S.6}

128. With regard to distribution of financial implications, the Central Government is to draw up the capital and recurrent expenditure for the implementation of the provisions of the Act in consultation with the State Governments. The Central Government is also mandated to provide grants-in-aid to State Governments and the rest of the expenditure is to be made by the State Government from its own resources. Determination of the grants-in-aid shall be made after consultation with the State Governments. However, the Central Government may make a reference to the Finance Commission under Article 280 (3) (d) to examine the need for additional resources for a State Government so that the State Government may provide for its own share of funds.\footnote{S.7 (4)}

129. Provisions with regard to finance hint at a situation that the Central Government has imposed an obligation on the States by way of the this legislation and that it has agreed to fund some of the financial implications according to its estimates after consultation with the State Government or the estimates of the Finance Commission.

130. With regard to other responsibilities, the legislation seem to fit the pattern of
the legislations on education discussed in the previous sections of this study. The Central Government has the responsibility of coordinating the standards of education, and providing technical support.\textsuperscript{153} This does reserve all fields for the Central Government for the purposes of designing the standards. Under S. 29 the ‘appropriate government has the responsibility’ of setting up an academic body for laying down the curriculum and evaluation procedure of elementary education at least.

131. It can at least be concluded that the legislation reserves a central role for the Central Government, but stipulates that most decisions are to be taken in consultation with the State Government. The area for the kinds of disputes witnessed in the context of the AICTE and NCTE Act seems to remain open under this legislation too, but to a smaller extent. Such disputes may arise in the limited context of whether the local authority or the appropriate government feels the necessity to establish schools in a particular area or not.

4. Other Relevant Legislations

a. National Rural Employment Guarantee Act (hereinafter NREGA)

132. Implemented by the Ministry of Rural Development, the NREGA “aims at enhancing livelihood security of households in rural areas of the country by providing at least one hundred days of guaranteed wage employment in a financial year to every household whose adult members volunteer to do unskilled manual work.”\textsuperscript{154}

133. According to the Government of India the “NREGA is the first ever law internationally, that guarantees wage employment at an unprecedented scale. The primary objective of the Act is augmenting wage employment. Its auxiliary objective is strengthening natural resource management through works that address causes of chronic poverty like drought, deforestation and soil erosion and so encourage sustainable development. The process outcomes include strengthening grassroots processes of democracy and infusing transparency and accountability in governance.”\textsuperscript{155}

134. The Act has attracted attention from various quarters on a host of issues. This study however, restricts itself to aspects of the Act which involve issues

\begin{flushright}
\textsuperscript{153} S. 7 (6) \\
\textsuperscript{154} National Rural Employment Guarantee Act, \url{http://india.gov.in/sectors/rural/national_rural.php} (Last visited on 19th December, 2009) \\
\textsuperscript{155} National Rural Employment Guarantee Act, available at, \url{http://india.gov.in/sectors/rural/national_rural.php} (Last visited on 19th December, 2009) 
\end{flushright}
of federalism. In doing so, we focus on two important aspects. First, the manner in which it distributes powers and responsibilities between different sets of government. Secondly, the fact that it charts out an important role to be played by the Panchayats.

What does the Act do?

135. The NREGA guarantees employment for the unemployed in rural areas for 100 days in a year, through work such as building roads, improving water supply and works that are necessary to improve infrastructure in rural areas. The Act is unique in the sense that it lays emphasis on issues of equality of wages for men and women, elimination of work contracting/middlemen, payment of wages only through bank and post office accounts to prevent corruption, creating transparency in workers muster rolls etc. The act guarantees that if work is not provided within a 15 day time frame (including the eligibility verification and issuing of the job cards) then the applicant is eligible for unemployment allowance. “The emphasis is on unskilled manual labour focusing on building roads and other public village infrastructural facilities, water conservation, afforestation, land development & drought proofing. If the work site is not within 5 kilometres from the applicant's residence then the applicant is eligible for an additional 10% of the wage”.

Distribution of powers and responsibilities between two levels of government

136. The powers and duties for implementing the Act are vested both in the Central Government and the State Governments. It requires vigorous co-ordination between both the levels of government to implement the Act.

137. Chapter II of the Act deals with guarantee of rural employment to households, which requires the State Government to provide at least one hundred days of guaranteed wage employment in a financial year to every household whose adult members volunteer to do unskilled manual work. It also lays down that either the Central Government or the State Government can prepare a scheme which extends beyond the guaranteed period.

138. Chapter III deals with the rules that the State Government has to follow while preparing a scheme for the hundred days of guaranteed employment. Under section 5, the State Government can specify the conditions for providing guar-

157 Ibid.
158 Ibid.
159 NREGA, S. 3(1).
anteed employment, without prejudice to the conditions specified in Schedule II. But it is the Central Government, who can notify the wage rate for the purposes of this Act; however it should not be at a rate less than sixty rupees per day. Also, until the Central Government specifies the wage, the minimum wage fixed by the State Government under section 3 of the Minimum Wages Act, 1948 for agricultural labourers, shall be considered as the wage rate applicable to that area.

139. Section 7 deals with payment and allowance and states that the terms and conditions for eligibility are to be provided by the State Government. Also the rate and procedure of the unemployment allowance is to be specified by the State Government, in consultation with the State Council. Subsection 3 provides the cases where the liability of the State Government to pay unemployment allowance will cease.

140. The Act also provides for two councils - the Central Employment Guarantee Council (hereinafter CEGC) and the State Employment Guarantee Council (hereinafter SEGC). The functions of the CEGC include establishing a central evaluation and monitoring system, advising the Central Government on all matters concerning the implementation of this Act. It reviews the monitoring and redressal mechanism and recommends steps required for improvement. It is should promote the widest possible dissemination of information about the Schemes made under this Act and prepare annual reports to be laid before Parliament by the Central Government on the implementation of this Act. The CEGC also has the power to undertake evaluation of the various Schemes made under this Act and for that purpose collect statistics pertaining to the rural economy and the implementation of the Schemes.

Section 12(3) prescribes the duties and functions of the State Council, which includes advising the State Government on all matters concerning the Scheme and its implementation in the State; (b) determining the preferred works; (c) reviewing the monitoring and redressal mechanisms from time to time and recommending improvements; (d) promoting the widest possible dissemination of information about this Act and the Schemes under it; (e) monitoring the implementation of this Act and the Schemes in the State and coordinating such implementation with the Central Council; (f) preparing the annual report to be laid before the State Legislature by the State Government; (g) any other duty or function as may be assigned to it by the Central Council or the State Government. The State Council also has the power to undertake an evaluation of the Schemes operating in

\[160\] Ibid, S.11.
Distribution of Costs

141. This Act also provides for the establishment of two funds- the National Employment Guarantee Fund and the State Employment Guarantee Fund. Section 22 lists the funding pattern. It provides that the Central Government has to meet the cost of:

(a) amounts required for payment of wages for unskilled manual work under the scheme;
(b) up to three-fourths of the material cost of the Scheme including payment of wages to skilled and semi-skilled workers subject to the provisions of Schedule II;
(c) such percentage of the total cost of the Scheme as may be determined by the Central Government towards the administrative expenses, which may include the salary and allowances of the Programme Officers and their supporting staff, the administrative expenses of the Central Council, facilities to be provided under Schedule II and such other item as may be decided by the Central Government.

The State Government has to meet the cost of unemployment allowance payable under the Scheme; one-fourth of the material cost of the Scheme including payment of wages to skilled and semi-skilled workers subject to the provisions of Schedule II, and the administrative expenses of the State Council.

Power to give directions

142. Section 27 says that the Central Government has the power to give directions to the State Government for the effective implementation of the provisions of this Act. It also has the power to cause an investigation, if it receives any complaint regarding the proper utilization of funds, in respect of any Scheme, and can also order stoppage of release of funds to the Scheme and institute appropriate remedial measures for its proper implementation within a reasonable period of time.

The Role of Panchayats

143. (a) The Act charts out an important role for Panchayati Raj Institutions in planning, monitoring and implementation. Section 13 provides that Panchayats...
at district, intermediate and village levels shall be the principal authorities for planning and implementation of the Schemes made under this Act. It also lays down the various functions of the Panchayats at the three levels. Section 13(4) says that the District Programme Coordinator will assist the Panchayat at the district level in discharging its functions under this Act and any Scheme made there under. Also the State Government can delegate any administrative and financial powers to the District Programme Coordinator as may be required to enable him to carry out his functions under this Act.

143 (b). Section 18 deals with the responsibilities of the State Government, stating that the State Government will have to make available to the District Programme Coordinator and the Programme Officers, the staff and technical support as required for the effective implementation of the Scheme. Also according to Section 23, the District Programme Coordinator and all implementing agencies in the District shall be responsible for the proper utilization and management of the funds placed at their disposal for the purpose of implementing a Scheme.

143 (c). Section 19 provides that the State Government will have to make rules and determine the appropriate grievance redressal mechanisms at the block level and the district level. It shall also lay down the procedure for disposal of such complaints.

143 (d). The Act therefore makes use of the different tiers of government to implement employment guarantee schemes. An interesting aspect is that the Union Parliament has prescribed the role to be played by the Panchayats and thus, does not leave it open to the State Government to determine the limits of that role.

Flaws in making the Act operational

144. Researchers have pointed out a number of flaws highlighted by the implementation of the Act. Though such flaws do not have a direct bearing on Centre-State relations, they might provide lessons for other areas where the three tiers of government seek to work together. One problem with the Act is the absence of clear remedies against infringements of the Act. Jean Dreize and Siddhartha have concluded that “(t)he NREGA talks the language of rights but there is virtual silence on available remedies when rights are violated. So far, the Central and State Governments have failed to put in place any system to respond to people’s complaints. Interesting ideas have been
floated, such as the appointment of ombudsmen or the activation of Lok Adalats, but they are yet to see the light of day.” 161

145. Another problem brought to the limelight is the lack of independent monitoring of the NREGA, whether in the States or at the Centre. Implementation of the Act has shown that both the CEGC and SEGC have proved to be non-functional bodies.162

146. But the most glaring flaw in the NREGA seems to be that there is “a troubling lack of clarity about the various actors’ basic responsibilities under the NREGA”.163 Under the Act, directions are given to every State Government to notify an “employment guarantee scheme” to give effect to the work guarantee. The amalgamation of a Central Act with State-specific schemes (and generally, the complex Centre-State relations behind the NREGA) requires a rigorous coordination between Central and State Governments. But this does not seem to happen in reality. “To illustrate with an example the Union Ministry of Rural Development does not even have a copy of each of the State schemes. The result is a confusing duality in the source of norms.” 164

147. Another study conducted by Participatory Research in Asia (PRIA), a NGO, revealed that most of the States have failed in providing mandatory 100 days of employment to each rural household. Even the government data corroborated the fact that only 44 days of employment have been provided across the country to each rural households.165

162 Ibid.
163 Ibid.
164 Ibid.
Report of the Commission on Centre-State Relations
Application of the Emergency Provisions since 1985

Constitutional democracies of the world do control emergencies both legally and politically. Political is more efficient and acceptable than legal.

— Mark Tushnet

148. Democracies throughout the world contain special Constitutional provisions designed to meet emergencies. Yet, since these provisions, by their nature, breach the Centre-State equilibrium by granting excessive powers to the Union in certain circumstances, the powers that they afford to Government are clearly circumscribed, for use with circumspection in extraordinary situations. While India’s Constituent Assembly underlined the inevitability of emergency provisions, it also expressed the hope that these would never be used.

149. Part XVIII of the Indian Constitution addresses emergencies in India: it envisions different forms of emergencies, with appropriate schemes to meet them all. Judicial decisions on the matter have further defined the emergency powers of government. The Sarkaria Commission Report and the Study of the National Commission to Review the Working of the Constitution provide a background of the Indian Constitution’s emergency provisions. Chapter VI of the Sarkaria Commission Report has a comprehensive account of the historical background and rationale of the emergency provisions in the Indian Constitution. Chapter 8 of the NCRWC Report deals with the Constitutional design of dealing with the failure of the Constitutional machinery as a part of the Centre-State relationship. A reading of both these documents also out-

167 See S. 119 of the Constitution of Australia, Article 16 of the Constitution of Switzerland, Article 91 of the West German Constitution, Article IV(4) of the Constitution of the United States.
168 S.R. Bommai, supra n. 13, at para 253, quoting Dr. Ambedkar from the Constituent Assembly Debates.
171 Union-State Relations, Chapter-8, available at http://lawmin.nic.in/ncrwc/finalstudy/v1ch8.htm, (Last visited on 16th December, 2009)
lines the areas where governments may abuse these provisions, launching the country or States into a state of emergency in order to obtain political benefits.

150. The ninth meeting of the Inter-State Council on August 27-28, 2003 recently examined the emergency provisions recommendations of the Sarkaria Commission and the NCRWC. It in turn recommended certain changes in the application of these provisions:

1. Article 356 should only be invoked as a last resort, where the Government has exhausted all alternative courses.

2. The Centre would have to issue a show cause notice to the State Governments before acting under Article 356. The notice requirement could be waived where immediate action is necessary to avoid ruinous consequence.

3. A Proclamation under Article 356 should not automatically dissolve the Legislature: Parliament should first accept it.

4. The safeguards corresponding to clauses (7) and (8) of Article 352 should be extended to Article 356.

5. The Governor’s report should be a ‘speaking document’ (i.e., should contain adequate reasoning).

1. Article 352: Proclamation of Emergency on Threat to National Security

151. Article 352 establishes grounds upon which the President may make a Proclamation of Emergency: “If the President is satisfied that a grave emergency exists whereby the security of India or of any part of the territory thereof is threatened, whether by war or external aggression or armed rebellion, he may, by Proclamation, make a declaration to that effect in respect of the whole of India or of such part of the territory thereof as may be specified in the Proclamation of Emergency.” The 44th Amendment, in fact, somewhat restricted this power, by inserting the expression “armed rebellion” in place of “internal disturbance”.

152. The Supreme Court has confirmed the more restricted scope of Article 352. In Naga People’s Movement of Human Rights v. Union of India, Justice Agarwal drew this distinction:

“The intention underlying the substitution of the word ‘internal disturbance’ by [sic] the word ‘armed rebellion’ in Article 352 is to limit the invocation of the emergency powers under Article 352 only to more serious situations where there is a threat to the security of the country or a part thereof on account of war or external aggression or armed rebellion and to exclude the invocation of emergency powers in situations of internal disturbance which are of lesser gravity.” 173

153. The judgment of the centre in assessing the situation in the States has been a contentious issue, especially where different political parties govern the Centre and the States. States also allege that Article 352’s Constitutional safeguard against misuse of Article 353 – parliamentary approval with a prescribed time schedule – is inadequate. The provision does not require for the Centre to consult with the States where they declare an emergency. Of course, such a consultation is not beyond the purview of the provision; consultation with the States would, in fact, be a healthy practice to follow in light of India’s federal spirit. Consultation would become all the more relevant in the cases where Parliamentary approval becomes even weaker: for example, where the Proclamation affects smaller States or States where regional parties rule.

2. Article 355: Duty of the Union to Protect the States

154. Article 355 is an expression of the duty of the Union to protect the States in a federal arrangement, and the Union can deploy its forces in States. The propensity of this Article to destabilise the federal arrangement was raised in the Constituent Assembly. Dr. Ambedkar addressed the concerns explaining that the ‘provinces are sovereign within their own field and if any invasion is done it should be based on this obligation of the Union.’ 174

155. The Union is to extend its help under three circumstances: external aggression, internal disturbance and to ensure that the government of the States is carried in accordance with the provisions of the Constitution. The imprecise nature of these expressions calls for attention.

156. The Sarkaria Report raises a concern with the scope of Article 355’s: the Union can send forces without any request from the States. The Sarkaria Report captures the delicate balance resting within the provision. On the one hand, it would be unwise to place States’ permission as a pre-condition of intervention by the Union. On the other, it would also be injudicious for the Union to use this provision to act on mere breach of public disorder.

173 Ibid, at para. 35.
174 CAD Vol. IX, p 133.
157. Article 355 is used sparingly. Recently, in September 2008, the Central Government issued directives to Orissa and Karnataka to contain the continued violence against Christians and Churches. The previous use of the provision was in 2002, where the Union issued a directive to the Gujarat Government on the Godhra incident. Apart from these, the invocation of this Article had been in 1968 and 1969, in the States of Kerala and West Bengal respectively. In Kerala, it was ostensibly to protect the offices and installations of the Union Government in the wake of unrest over the Education Bill and in West Bengal with the same purpose in the backdrop of a general strike and ensued violence.

158. Courts have not significantly addressed the interpretation of “external aggression” or “internal disturbances” and, thus have not particularly influenced Centre-State relations since 1985 in this respect.  

159. The Union’s third duty in Article 355, “to ensure that the Government of every State is carried on in accordance with the provisions of this Constitution”, also bears upon Article 356. The question as to the relevance and inter-relation of Article 355 (then Draft Article 277A) to other provisions relating to emergency in the Constitution were addressed in the Constituent Assembly Debates. It was made clear that Article 277A is not a mere pious declaration. In a federal Constitution where the provinces are sovereign in their own fields, any interference from the Centre in those fields will be unacceptable. At the same time, the Draft Constitution had Articles 278 and 278A (presently Articles 356 and 357) permitting intervention. Article 277A imposes a duty on the centre to protect the provinces and to maintain the Constitution. This authorises the Centre’s intervention. This is reflected in the following passage from Constituent Assembly Debates:

“[I]f the Centre is to interfere in the administration of provincial affairs, as we propose to authorise the Centre by virtue of Articles 278 and 278-A, it must be by and under some obligation which the Constitution imposes upon the Centre. The invasion must not be an invasion which is wanton, arbitrary and unauthorised by law. Therefore, in order to make it quite clear that Articles 278 and 278- A are not to be deemed as a wanton invasion by the Centre upon the authority of the province, we

175 Sarbananda Sonowal v. Union of India, AIR 2005 SC 2920, at paras 32-36 have attempted clarify the meaning of the expression ‘external aggression’ in the background of determining the Constitutional validity of Illegal Migrants (Determination by Tribunals) Act, 1983.

176 Ibid.
propose to introduce Article 277-A. As Members will see, Article 277-
A says that it shall be the duty of the Union to protect every unit, and
also to maintain the Constitution.”

160. S.R Bommai reviewed the ambit of Article 355 and held that it cannot be
construed as an independent source of power.  

“[I]t is clear from Article 355 that it is not an independent source of
power for interference with the functioning of the State Government
but is in the nature of justification for the measures to be adopted un-
der Articles 356 and 357.”  

On the interrelationship of Article 355 with Article 356, Sarkaria Com-
mission has expressed its views while answering the question, whether
every infraction of the state call for an interference by the centre, in the
following words

“[B]y virtue of Article 355 it is the duty of the Union to ensure that the
Government of every State is carried on in accordance with the provi-
sions of the Constitution. Article 356, on the other hand, provides the
remedy when there has been an actual breakdown of the Constitutional
machinery of the State. Any abuse or misuse of this drastic power dam-
gages the fabric of the Constitution, whereas the object of this Article is
to enable the Union to take remedial action consequent upon break-
down of the Constitutional machinery, so that governance of the State
in accordance with the provisions of the Constitution, is restored.”

161. The conviction of the Bommai court on the interrelationship, for which it re-
lies on the Sarkaria Report also, can be found in the following statement.

“Article 355 … imposes a duty upon the Union to protect the States
against external aggression and armed rebellion and also to ensure that
the Government of every State is carried on in accordance with the
provisions of the Constitution. Articles 355, 356 and 357 go together.

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177 From Ambedkar’s speech
178 For an alternate view of this position, see, Subhash C. Kashyap, Constitutional Law of India Vol. 2,
Universal, 2008, p 2209. It is argued that Article 355 has to be read as a self-contained code as the obligation
carries with it the power to discharge the Constitutional obligation to ensure that the governments of the
states are carried on in accordance with the Constitution. It is further stated that Article 355 should not be
treated as a mere prelude to imposition of President’s Rule under Article 356.
179 Para 57.
180 Para – 6.3.23
Article 356 provides for the action to be taken by the President where he is satisfied that a situation has arisen in which the Government of a State cannot be carried on in accordance with the provisions of the Constitution by making a Proclamation in that behalf, while Article 357 sets out the powers that can be exercised by Parliament when a Proclamation under Article 356 is in operation. Undoubtedly, breakdown of the Constitutional machinery in a State does give rise to a situation of emergency. Emergency means a situation which is not normal, a situation which calls for urgent remedial action. Article 356 confers a power to be exercised by the President in exceptional circumstances to discharge the obligation cast upon him by Article 355. It is a measure to protect and preserve the Constitution, consistent with his oath. He is as much bound to exercise this power in a situation contemplated by Article 356 as he is bound not to use it where such a situation has not really arisen."

Later in *Rameswar Prasad*81, the Supreme Court reiterated the *Bommai* position and held that the raison d’être of Article 355 was to control any unprincipled invasion by the Union in the affairs of the States. Articles 355 and 356 prescribe the circumstances under which Union can upset the fine balance of autonomy of the units.

162. The Sarkaria Commission and the National Commission on the Review of the Working of the Constitution have placed identical recommendation that all possibilities available to discharge the Constitutional duty of the Union under Article 355 may be exhausted before acting in pursuance of Article 356.

3. **Contentious issues in Article 356**

163. Article 356 has generated numerous political and legal mêlées in independent India. The number of times it has been invoked, and the debate over such use being justified, suggests that apprehensions about the misuse of this provision may have some legitimate basis.

164. A report from the Governor of a State enables the President to make a Proclamation under Article 356. However, the President is not precluded by the provision from issuing a proclamation without a report from the Governor. Such a situation has occurred only once when in 1991 the Karunanidhi Government was removed without a report from the Governor.82 Courts have not

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81 *Rameswar Prasad and Ors. v. Union of India (UOI) and Anr.* AIR 2006 SC 980
82 MP Singh, VN Shukla’s *Constitution of India*, (Lucknow: Eastern Book Company, 2008) at page 969
yet defined proper justification and the ability of the Courts to judicially review the government’s reasoning when it issues a proclamation. In *S. R. Bommai*, K. Ramaswamy J.’s opinion suggested some instances where to invoke Article 356 could be justified:

> “While it is not possible to exhaustively catalogue diverse situation when the Constitutional breakdown may justifiably be inferred from, for instance (i) large-scale breakdown of the law and order or public order situation; (ii) gross mismanagement of affairs by a State Government; (iii) corruption or abuse of its power, (iv) danger to national integration or security of the State or aiding or abetting national disintegration or a claim for independent sovereign status and (v) subversion of the Constitution while professing to work under the Constitution or creating disunity or disaffection among the people to disintegrate democratic social fabric.”

165. The Supreme Court drew attention to the indications provided by the Constitution itself like: the failure to comply with the directions given by the Centre (Article 365) and violation of stipulations under Article 257. The Court echoed the view of Ambedkar on the desirability of issuance of a forewarning before employing Article 356.

166. The Court also sketched the extent and limitation of the power under Article 356. To summarize:

- The power conferred in Article 356 is not absolute, but limited by expressions like: “on the receipt of report from the Governor of a State or otherwise”; “is satisfied” that “the situation has arisen in which the government of the State cannot be carried on”; and “in accordance with the provisions of the Constitution”.

- The Proclamation can only be issued on the *objective* satisfaction of the President (based on objective material) that unless the Proclamation is issued the government of the State cannot be carried on in accordance with the provisions of the Constitution. In this sense, not every constitutional breach calls for a Proclamation.

- With appropriate objective evidence, the President’s satisfaction is not open to question.

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165 *S.R. Bommai*, supra n. 13.

The expression “may” in the provision does not grant a discretionary power but rather imposes a duty to check the advisability and necessity of the action. It also involves an obligation to consider which of the several steps specified in sub-clauses (a), (b) and (c) should be taken and to what extent. Dissolution of the Legislative Assembly, for example, is not a matter of course, but should only be imposed where it is necessary to achieve the purposes of the Proclamation.

Both houses of Parliament must approve the exercise of the power. Clause (3) is both a check on the power and a safeguard against abuse of power.

Once the proclamation under Article 356 (1) is issued or simultaneously with it, the President can take any or all the actions specified in clauses (a), (b) and (c).

167. Despite the Supreme Court’s pronouncements, Article 356 needs to be further defined. Ramaswamy J.’s opinion, for example, is very broad in scope. The Sarkaria Commission rejected a “wide literal construction”. It is not every constitutional infraction that should call for an action under Article 356. The Article means “to take remedial action consequent upon break-down of the Constitutional machinery, so that that governance of the State in accordance with the provisions of the Constitution is restored.”

168. Judicial review of the Presidential proclamation is another unsettled issue. The 38th Amendment sought to bar the jurisdiction of the Court, but it was later repealed by the 44th amendment. It is now settled that Article 356 presidential orders can be judicially reviewed. The remaining issue, despite a number of judgments on it, is the scope of this review. In *Bommai*, the Supreme Court tried to strike a balance between the power of the executive with the need to review in certain circumstances, such as a *mala fide* exercise of the power. The court could not provide a clear picture of the width of judicial review. Justice P.B Sawant speaks about the existence of judicial review. Other opinions speak about the grounds that will give rise to judicial review and conditions, in the presence of which there shall not be any judicial review. A later case, *Rameshwar Prasad*, also offers little help to develop the scope and ambit of judicial review.

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185 Ibid, at para. 6.3.23.
186 Ibid, at para. 6.3.23.
187 Justices Verma and Ahmadi.
188 Justice Jeevan Reddy.
189 Supra n. 181.
The Sarkaria Commission recommends entrenching judicial review in the Constitution by a Constitutional amendment, whereas the NCRWC suggests development of conventions. NCRWC has also suggested two amendments to Article 365 in the same line as that of the Sarkaria Commission. The debate about the need of Article 356 and how it should be redesigned is still alive and relevant.

169. High courts have also attempted to define Article 356, with relatively minor success. In *H.S. Jain v. Union of India*, the Allahabad High Court examined the scope of Article 356(5), which prohibits continuance of the same Proclamation beyond one year. The government, already having proclaimed an emergency, had attempted to issue a second Proclamation, stretching the state of affairs beyond one year, arguing that this second proclamation revolved around a new issue. The High Court held that Article 365 prohibited the issuance of fresh proclamation in the current fact situation. The impugned proclamation may have been a fresh proclamation in form, but in substance and in effect was the continuation of the Presidential Rule without interregnum. An interpretation of Article 365 (5) allowing the fresh proclamation to have effect would have opened doors to continue the Proclamation without any constitutional checks.

170. The High Court of Gauhati in *Union for Human Rights and Ors. v. Union of India* emphasized the distribution of powers between the Centre and the States against the backdrop of the November 1990 Presidential declaration. The Central Government declared the entire State of Assam a disturbed area under the Armed Forces (Special Powers) Act, 1958 (armed forces would therefore be deployed to maintain law and order). Also, the Governor of Assam declared Assam a disturbed area under the Assam Disturbed Areas Act, 1955. The decision was subsequently overruled by the Supreme Court in *Naga People’s Movement of Human Rights v. Union of India*.

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190 Sarkaria Commission recommendation 6.6.25. “We recommend that to make the remedy of judicial review on the ground of *mala fides* a little more meaningful, it should be provided, through an appropriate amendment, that “notwithstanding anything in clause (2) of Article 74 of the Constitution the material facts and grounds on which Article 356 (1) is invoked should be made an integral part of the proclamation issued under that Article. This will also make the control of Parliament over the exercise of this power by the Union Executive, more effective.”

191 The Study 8.19.1 to 8.19.5.

192 The Study 8.21.3 and 8.21.4


195 Supra n. 172.
171. The Court had held since “public order” and “police” were subject-matters in the State List, the responsibility of the State Government in these two spheres should be respected. The Court also stated that Central Reserve Police Force, following within the category of “other Armed Forces of the Union”, could not exercise powers merely on the basis of the State’s notification under the Act of 1955. The notification under the State Act could only allow the Assam Police Force and Police Forces of other States if especially empowered under the Police Act of 1888 to exercise powers with regards to the disturbed areas in the State of Assam.

172. High Court decisions suggest that there may be alternatives to the Supreme Court’s current emergency provisions interpretation, interpretations that would be more restrictive of the broad Union power and more considerate of State concerns.

V. ENSURING BETTER REPRESENTATION FOR STATES WITH SMALLER POPULATIONS

173. Matters pertaining to elections exercise some influence on the relationship between the Centre and the States. The primary reason for this influence is the fact that under our constitutional scheme, the Centre can influence and even act on matters pertaining to the States. It can also, under certain circumstances, exercise powers which are otherwise within the exclusive domain of the States. Given this reason, it is important for the States to have adequate representation at the Centre and questions of representation in our political institutions are primarily addressed by elections.

174. Representation is a manner of ensuring the participation of people in matters which affect them. Some matters only affect particular states while others have interstate characteristics or constitute matters of national importance. Through two major federal devices, the Indian Constitution tries to ensure a voice for the people of particular States in matters that impact their own State and in general matters of national importance:

1. Division of legislative power and fields of legislation.
2. Ensuring representation of the States at the Centre.

196 Our answer to this question substantially relies on the note that we had submitted to the Commission on Centre-State Relations in January 2009.
197 Article 249 is a clear instance of exercise of such power.
198 This is by reserving those matters for states which primarily affect the States, the general theory being that matters of national importance are addressed by the Parliament.
175. We have already discussed the division of legislative powers above. We now expand on the representation of States at the centre. Should the commission determine that States require more representation in the centre, there would appear to be two ways of bringing about such a change:

1. Amending the Constitution to give more decision making powers to the States.

2. Making the representation of the States at the Centre more real and doing the same in a manner that rationally connects it to the objectives.

176. This part of the study explores the latter option, since it seems to be a more plausible and convenient method of bringing changes without requiring substantial changes to the text of the Constitution. The first route is would require major changes in important provisions of the Constitution. The second route would only require making certain minor amendments to the Constitution and change in electoral processes, towards which the Constitution has already made certain gestures. In the sections that follow, some suggestions along the second route are made.

177. The suggestions below do not deal with those important questions of electoral reforms which do not appear to have an impact on Centre-State relations. Prominent examples in this category include recommendations of the Law Commission on the ‘first past the post system’, introduction of the ‘list system’, and intra-State delimitation.

178. The suggestions primarily try to highlight and tackle issues arising out of the relationship between the population of States and the number of representatives a State has in the House of the People and the Council of States. This is set upon the backdrop of the argument for a federalism which warrants real power for the States and truly federal practices without interfering with the present Constitutional scheme. The first set of suggestions engages with the problem of the mismatch between States with lesser populations (including those who have successfully implemented family planning measures) and their representation in the two houses. The second set of suggestions makes a case for watering down the emphasis of the linkage between the population of a State and the number of representatives it has in the Rajya Sabha. The third
set of suggestions is with regard to the domiciliary requirements for the Rajya Sabha.

1. **Amending the proviso to Article 81 (1) (2)**

179. Due to the freezing of the population to the 1971 census, for purposes of Article 81 (2)(a), States who have been able to successfully implement family planning measures stand to lose out on the number of seats they have in the Lok Sabha as compared to the States whose populations continue to increase. This means that the States with the reduced and controlled population would have a lesser say in terms of votes. These States may have signed on to the Constitution with the understanding that they would be sufficiently represented in the Lok Sabha. In order to address this issue it is important (for political or Constitutional reasons) to ensure that the States with lesser populations do not lose on their political voice as a consequence of achieving desirable policy objectives. According to certain predictions, if the present situation continues, then, by 2016, the States in northern India would have 270 seats instead of the 239 that they have now; the States in Southern India would have only 108 seats instead of the 129 that they have now. 199

180. Any Constitutional measure to address this problem would not be completely a novel one as the proviso to Article 81 (2) has already created an exception to the general rule set out in the sub clause in order to ensure adequate representation of States with populations below six million. It is suggested that those States which have reduced or controlled their population over the years should also be included in the proviso to benefit from the exception created. This suggestion acts as an alternative to the solution of freezing the number of Lok Sabha seats. Freezing seats appears to affront the basic tenets of indirect democracies, and may also require a Constitutional amendment, which would render Article 81 (1) (a) redundant.

2. **Reallocation of seats in the Rajya Sabha**

181. A quick survey of other federations with a bicameral arrangement, reveals that while the Lower House typically links representation to population, the Upper House often links representation to territory, irrespective of the population. Delinking population from representation in the upper house aims to offset the sway that larger States could have in both houses. This is particu-

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larly true in multination countries. During negotiations over a country’s constitution, bicameralism can help to include sub-national entities in national decisions by representing them in an upper house, so that national decisions will satisfy their concerns. Where minorities in a country are concentrated in the smaller sub-entities of a federal system, the upper house may overrepresent these sub-entities, to force the majority to account for their concerns. This is done in Spain, for example, where the Spanish Senado represents provinces equally (by apportioning an equal number of senators to each), regardless of population. Smaller provinces are overrepresented while larger provinces are underrepresented.

182. The Canadian and the U.S. Senate also equally represent geographical units. The Canadian Senate represents provinces equally while the U.S. Senate represents states equally. In both cases, equal representation came as a result of a political compromise. Because they believed in their distinct identities, smaller units were unwilling to enter confederation unless they received a guarantee that they would be equally represented in the upper house. Without overrepresentation for smaller sub-entities, countries like Canada and the U.S. may never have existed: overrepresentation for less populated regions in Canada and states in the U.S., despite a possible lack of theoretical basis, ensured their participation in the federation. In India, this idea of political compromise, regardless of any potential theoretical basis, may be worthwhile if it ensures national unity.

183. The Constitutional framework of the composition of the Rajya Sabha in India (Article 80) does not necessarily link population with the number of seats. Schedule IV details the number of seats that each State has, though in practice it has worked out the scheme on the basis of population: the formula is one seat for a population of each million for the first five million and then a seat each for every next two millions. This formula is infused with a system of

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200 In Canada, George Brown stated before the Canadian Legislative Assembly on February 8, 1865: “Our Lower Canadian friends have agreed to give us representation by population in the Lower House, on the express condition that they could have equality in the Upper House. On no other condition could we have advanced a step”: Parliamentary Debates on the Subject of the Confederation of the British North American Provinces (Quebec: Hunter, Rose, 1865) at 88. In the U.S. the Philadelphia Convention elected a committee to frame a compromise over representation in the Senate. The committee reported back on July 5, proposing that while each state would have an equal vote in the Senate, all bills of appropriation would stem from Congress and not amendable by the Senate. This arrangement became known as the Great Compromise: Jack N. Rakove, Original Meanings: Politics and Ideas in the Making of the Constitution (New York: Vintage Books, 1996) at 70 (Rakove argues that the compromise was in fact a defeat of the larger states since the bill of appropriation concession was meaningless).
weighted representation which is expected to address the interests of States with relatively less population. The justification of weighted representation is the same as that of other federations mentioned earlier with an addendum that equal representation for all would have made the will of the minority overpower the will of the majority.

184. If federalism aims to ensure rational distribution of power and States’ involvement in the governance of the nation, two Houses of Parliament can also play this role. Since the Lok Sabha is directly linked to the population (read with the proposal made earlier), delinking the relation between population and number of seats per States/Union Territories would only create a balance of power between the different constituents in the federation.

185. Alternatively, it could be argued that since larger States and States with relatively higher population already have more representatives in the Lok Sabha, the Rajya Sabha could be a place where the States as the constituents of federation have equal say irrespective of the size and population.

186. The fact of weighted representation is not an alien concept to our Constitutional scheme, as it has already been a part of Article 80 and 81. The proposed change could be made by amending Schedule IV.

3. **Domicile requirement**

187. Federations aim to accommodate plurality and coexistence with shared powers of governance. One of the aspects of federalism is participation of the constituent units in the central decision-making process. This participation is ensured through different modes. Two such approaches are: 1) compositional arrangement for sub-units’ representation in legislatures and cabinets, 2) relational arrangement by having a body specifically linked to States that interacts with other bodies of the Centre. An upper house, for example, could be designed as an example of the second approach. The federal arrangement of our nation reflects both approaches.

188. Ultimately, allowing constituent units to participate in the central decision-making seeks to prevent domination of one component of the federation over the other. The principle of federalism animates this objective and can often justify those political arrangements that promise equilibrium.

189. The value of a second chamber is to give appropriate participation to the units of the federation in the central decision-making process. It can arrest
the centrifugal tendencies of the Centre by giving a say to the representative of the States in the national legislature. These representatives fight against the perils of undue centralization in two fashions. First, representatives can limit the extent of the Central Government’s power (for example, by declining Central Government jurisdiction over matters of contention between State and Centre). Second, representatives can reflect the interests of the States in the creation of national policy.

190. Clearly, then, if the Upper House is meant to vouch for the interests of States, the composition of this house is a matter of importance. Where States have good representatives in the upper house, their interests will be vindicated. However, where States do not have good representation or where they do not have representation at all, it will be difficult to suggest that the upper house will properly defend State interests. Worldwide, the composition and manner of representation has become an indicator of federalism (though in India the Kuldip Nayar held otherwise). It has become expected that the Upper House should reflect the interests of the sub-units and provide checks and balances against the exercise of power by the central authorities that might affect the interests of the constituents.

191. The position of the Rajya Sabha in the context of federalism and Centre-State relationships in India, therefore, is critical.

192. The law as it stood before the Representation of People (Amendment) Act 40 of 2003, had stipulated an inevitable territorial link between the representative of the Rajya Sabha and the State which they represent. The law had prescribed that one of the qualifications to become the representative of a particular State in the Rajya Sabha was being an elector of a Parliamentary constituency in that State. The purpose of this provision was to ensure that the person who represented the State had a territorial nexus to the State, and thereby an interest in the affairs of the State.

193. The 2003 amendment to the Representation of People Act, 1951 (RP Act) severed this territorial nexus by providing that the candidate could be an elector of a Parliamentary constituency in India.

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202 Kuldip Nayar, supra n. 19, at para 39.
203 S. 3 as it originally stood reads thus; 3. Qualification for membership of the Council of States. - (1) A person shall not be qualified to be chosen as a representative of any Part A or Part B State (other than the State of Jammu and Kashmir) in the Council of States unless he is an elector for a Parliamentary constituency in that State … (Emphasis added)
204 The amended section stands as; 3. Qualification for membership of the Council of States. - A person shall not be qualified to be chosen as a representative of any State or Union territory in the Council of States unless he is an elector for a Parliamentary constituency in India … (Emphasis added)
elector from any of the Parliamentary constituencies of the nation. The reason for this amendment is clear: it was to facilitate the election of certain persons to Rajya Sabha and to legitimize some past actions of violation of Section 3, which were being challenged.

194. Since India is considered a federation with a strong centre, the Representation of People (Amendment) Act’s move in August 2003 to delink territorial nexus of representation in the Rajya Sabha seems suspect, particularly because it appeared to pass for reasons of mere expediency.

195. There is literature in other countries (the U.S., for example) that suggests that Upper Houses, although they initially aimed (1) to represent the interests of the States (2) to better coordinate the constituent units of the federation and (3) to check and balance these units, have in practice turned into national institutions. The present position of the law in the Representation of People Act, only augments such an unhealthy tendency.

196. The relevance of the need for a link between domicile and representation in the Rajya Sabha can be seen in some of the functions of the Rajya Sabha, to illustrate, Article 249(1). This Article enables the Parliament to legislate on the fields earmarked for the States in List II of Schedule VII.

197. The present position of the law poses questions regarding the nature of Indian federalism. As the very name suggests, the Rajya Sabha, “Council of States”, seeks to determine and protect the interests of the States. The Rajya Sabha locates and balances these interests in the larger milieu of the national interests. It is designed to give an opportunity to ventilate the claims and concerns of the States where the centre legislates on matters that could have a direct and indirect bearing on the States and Union Territories. This makes a case, for maintaining a direct link between the representative and the territory which they are representing. This argument however, is contrary to the current position in law.
Appendix 1

The table below shows the invocation of emergency provisions in reverse chronological order from 2009.

<table>
<thead>
<tr>
<th>Year</th>
<th>Govts. Involved</th>
<th>Articles invoked</th>
<th>Reason Stated for Declaring Emergency</th>
<th>Case if any</th>
</tr>
</thead>
<tbody>
<tr>
<td>March 18, 2009</td>
<td>Meghalaya: Donkupar Roy (CM) United Democratic Party United Democratic Party (UDP) / (MPA)</td>
<td>Article 356.</td>
<td>NCP-led MPA Government won the trust vote in the assembly amid uproar and alleged partisanship showed by the Speaker. The MPA Government had survived the trust vote with the help of the single vote cast by the Speaker. Governor Ranjit Shekhar Mooshahary has reportedly recommended President's Rule in the State, saying there is a breakdown in the constitutional machinery.</td>
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<tr>
<td>January 19, 2009</td>
<td>Jharkhand: Shibu Soren (CM) Jharkhand Mukti Morcha (JMM)</td>
<td>Article 356(1)</td>
<td>President's rule was imposed in Jharkhand, after Chief Minister Shibu Soren resigned. Soren resigned following his defeat in the Tamar Assembly bypoll, plunging the</td>
<td></td>
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</tbody>
</table>
State into political instability. The Governor’s report mainly cited political instability as the reason for imposing President’s Rule. He is understood to have described the prevailing political scenario in Jharkhand where no political party appears to be in a position to form a stable government.

<table>
<thead>
<tr>
<th>Date Range</th>
<th>Location/Party Details</th>
<th>Article 356(1)</th>
<th>Reference</th>
</tr>
</thead>
<tbody>
<tr>
<td>January 3, 2008</td>
<td>to March 12, 2008</td>
<td>The Democratic Alliance of Nagaland/Nagaland People's Front-Nagaland (regionalist) (DAN)/(NPF)</td>
<td>Yitachu v. Union of India (UOI) and Ors. [AIR2008Gau103]</td>
</tr>
<tr>
<td>November 20, 2007</td>
<td>Karnataka B.S. Yeddyurappa (CM) Bhartiya</td>
<td>BJP's refusal to accept Janata Dal-Secular's (JD-S)</td>
<td></td>
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<tr>
<td>Date</td>
<td>Party/Coalition</td>
<td>Event</td>
<td>Reference</td>
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<tr>
<td>May 30, 2008</td>
<td>Janata Party (BJP)</td>
<td>latest demands to sign a new power-sharing deal allotting plum ministerial portfolios to it. The BJP government in Karnataka collapsed following coalition partner JD-S decision to vote against the Government's confidence vote in the Assembly. After JD-S refused to vote for BJP, Yeddyurappa announced his decision to quit in the House and submitted his resignation to the Governor, who then recommended imposition of President's rule in the State.</td>
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</tr>
<tr>
<td>October 6-12, 2007</td>
<td>Karnataka: H.D. Kumaraswamy (CM), Janata Dal-Secular (JD-S)</td>
<td>Article 356(1) H.D. Kumaraswamy quit after his government was reduced to a minority as his coalition partner, the Bharatiya Janata Party (BJP), withdrew support from the coalition arrangement. The BJP pulled out of the coalition when Kumaraswamy refused to hand over power to it for</td>
<td>Syed Mudir Agha v. State of Karnataka, rep. by Principal Secretary and Ors, [2008(5) KarLJ 378]</td>
</tr>
<tr>
<td>Date Range</td>
<td>State/Party</td>
<td>Article/Case/Citation</td>
<td>Description</td>
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</tr>
<tr>
<td>March 7, 2005 to</td>
<td>Bihar: Rabri Devi (CM), Rashtriya Janata Dal (RJD), (regionalist)</td>
<td>Article 356(1)</td>
<td>The President’s Rule was imposed eight days after elections had thrown up a hung Assembly in which Government formation was not possible. Governor Buta Singh gave a report to the Centre saying no political party or group was in a position to form a stable government. He also dissolved the outgoing 12th state Assembly hours after recommending imposition of President’s rule.</td>
</tr>
<tr>
<td>November 24, 2005</td>
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<td></td>
<td>Rameshwar Prasad v. Union of India [ AIR 2006 SC 980]</td>
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<tr>
<td>4 Mar 2005 -</td>
<td>Goa: Pratapsing Rane(CM) Indian National Congress (INC)</td>
<td></td>
<td>The President’s Rule was imposed after the Pratapsing Rane led Congress government in Goa won a controversial trust vote. The House voted 17-16 in the government’s favor, with Speaker</td>
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<td>7 Jun 2005</td>
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<tr>
<td>Francisco Sardinha casting his vote after there was a tie. United Goans Democratic Party legislator Mathany Saldhana was restrained from voting by the Speaker by passing an ad-interim order. According to Home Minister, Mr. Sivraj Patil, it was not proper not to allow one member to vote and then get the Confidence Motion passed with a casting vote given by the Speaker. The general view in the Cabinet was that the manner in which the vote of confidence had been secured was &quot;not tenable.&quot;</td>
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<tr>
<td>Date</td>
<td>State</td>
<td>Political Party Leader</td>
<td>Political Party</td>
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<tr>
<td>June 2, 2001 to March 5, 2003</td>
<td>Manipur</td>
<td>Radhabinod Koiriam (CM)</td>
<td>Samata Party</td>
</tr>
<tr>
<td>March 8, 2002 to May 3, 2002</td>
<td>Uttar Pradesh: Rajnath Singh(CM) Bhartiya Janata Party BJP</td>
<td>Article 356(1) President’s rule was imposed because the single largest Samajwadi Party was not in a position to muster majority for government formation. The election results showed that the mandate of the voters was fractured and no single party was in a position to individually form a stable Government; on 26-2-2002, the Bahujan Samaj Party (BSP) informed Governor of Uttar Pradesh that B S P will not support Mr. Mulayam Singh Yadav of Samajwadi Party (SP) to form the Government. Mr. Mulayam Singh Yadav met the Governor and staked his claim to form the Government, on which the Governor asked him to furnish a list of the members supporting his claim but he did not furnish the same. Mr. Raj Nath Singh, leader of the Vidhan Mandal Dal of BJP</td>
<td>Social Action for People's Rights and Anr. Vs. State of Uttar Pradesh [AIR2003All250] [Note: this case does not deal directly with the imposition of President’s rule, but deals with whether the appointment of Mayawati as CM, after the President’s rule was revoked, was Constitutional or not.]</td>
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<tr>
<td>Date Range</td>
<td>Location</td>
<td>Event</td>
<td>Article</td>
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<tr>
<td>February 10, 1999 to June 9, 1999</td>
<td>Goa; Luizinho Faleiro Indian National Congress (INC)</td>
<td>the Governor and apprised him that BJP had decided not to support any party. Also, the President of Rashtriya Lok Dal informed the Governor that his party would not support the SP in formation of the Government. In these circumstances. The Governor sent his report to the President of India, who on 8-3-2002 issued a proclamation under Article 356 of the Constitution.</td>
<td>Article 356(1)</td>
</tr>
<tr>
<td>February 12, 1999 to March ,8</td>
<td>Bihar; Rabri Devi(CM) Rashtriya Janata</td>
<td>The government was dismissed by the</td>
<td>Article 356(1)</td>
</tr>
<tr>
<td>Year</td>
<td>Party</td>
<td>Reason</td>
<td>Case</td>
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<tr>
<td>1999</td>
<td>Dal (RJD)</td>
<td>President on the ground of the failure of the civil administration to maintain law and order situation in Bihar. The Governor’s report listed a series of acts of omission and commission on part of the State Government, as constituting a breakdown of Constitutional machinery in the State, in the wake of the macabre cruelty exhibited by the Ranbir Sena, slaying many dalits including women and children. But the proclamation was revoked since the government knew that it could not be passed in the Rajya Sabha, where they were in a minority.</td>
<td>Union of India (UOI) and Ors. [AIR1999Pat221]</td>
</tr>
<tr>
<td>September 19, 1996 - October 23, 1996</td>
<td>Gujarat: Suresh Chandra Mehta (CM) Bharatiya Janata Party (BJP)</td>
<td>Article 356(1) President’s Rule was imposed but the legislature was kept suspended. The controversy centred around the vote of confidence “won” by the BJP with 92 votes to nil in the 182-member House with an effective strength of 179.</td>
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</tbody>
</table>
voting was preceded with unprecedented bedlam and violent scenes, during which the opposition members, including some independents, were evicted from the House. In his report, the Governor had expressed doubts about the Chief Minister’s claim of majority support in the Assembly.

| October 17, 1996 to March 21, 1997 | Uttar Pradesh | Article 356(1) | President’s Rule was imposed in UP with the suspension of the Assembly on the ground that no party or group was in a position to form a stable Government. In a House of 425 members, the single largest party BJP, and its allies had a strength of 179 and it staked claim for the formation of ministry. However, Governor Ramesh Bhandari felt that:
  i) The BJP did not have majority support,
  ii) It was not clear about where from it could get the necessary support, and |

| |
| H.S. Jain and Ors., etc. Vs. Union of India (UOI) and Ors., etc. [(1997)1UPLBEC 594] |
### Application of the Emergency Provisions since 1985

<table>
<thead>
<tr>
<th>Date</th>
<th>Location</th>
<th>Party Leader(s)</th>
<th>Article 356(1)</th>
</tr>
</thead>
<tbody>
<tr>
<td>October 18, 1995 to March 21, 1997</td>
<td>Uttar Pradesh, Mayawati(CM) Bahujan Samaj Party (BSP)</td>
<td>Article 356(1) The BJP-BSP Government headed by Ms. Mayawati fell, when the BJP withdrew its support to the government. The claim of BJP to form a fresh government was neither allowed nor considered. The Governor reported that no viable ministry was possible, and hence the President’s rule was imposed.</td>
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<tr>
<td>March 28, 1995 to April 24, 1995</td>
<td>Bihar: Laloo Prasad Yadav(CM) Rashtriya Janata Dal (RJD)</td>
<td>Article 356(1) President’s Rule was imposed in the State of Bihar to enable the Parliament to fulfil a Constitutional obligation of approving the expenditure for the State beyond 31 March 1995 as the</td>
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</tr>
<tr>
<td>Date Range</td>
<td>State</td>
<td>Political Leaders</td>
<td>Events/Remarks</td>
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<tr>
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<tr>
<td>December 31, 1993 to December 13, 1994</td>
<td>Manipur</td>
<td>Raj Kumar Dorendra Singh (CM) Indian National Congress (INC)</td>
<td>Article 356(1) The coalition ministry headed by the Congress(1) leader R.K. Dorendra Singh could not combat the law and order problem effectively. In the wake of continued Naga-Kuki clashes and a rising number of attacks on security forces, resulting in about 1000 deaths, President’s Rule was imposed in the State. The Assembly was placed in a State of suspended animation.</td>
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<tr>
<td>March 11, 1993 to April 10, 1993</td>
<td>Tripura</td>
<td>Samir Ranjan Barman (CM) Indian National Congress (INC)</td>
<td>President’s Rule was imposed in Tripura when the term of the Tripura Assembly had expired and the election could not be held because it was postponed by</td>
</tr>
<tr>
<td>Date Range</td>
<td>Location</td>
<td>Article</td>
<td>Event Description</td>
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<tr>
<td>April 2, 1992 to February 22, 1993</td>
<td>Nagaland: Vanuoso Phesao (CM) Indian National Congress (INC)</td>
<td>Article 356(1)</td>
<td>The government fell when 12 members of Nagaland People’s Council withdrew support, accusing the CM of mismanaging funds. The CM recommended the dissolution of the Assembly which was accepted later. The Governor’s Report said that the ruling party in the State had failed and the administration of law and order had been neglected. Hence the President’s rule was imposed.</td>
</tr>
<tr>
<td>Date Range</td>
<td>State/Party Details</td>
<td>Article 356(1)</td>
<td>Explanation/Case Reference</td>
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<tr>
<td>January 7, 1992 to</td>
<td>Manipur:</td>
<td>The 6 party United Legislature Frontheaded by R.K. Ranbir Singh was reduced to</td>
<td>The 6 party United Legislature Frontheaded</td>
</tr>
<tr>
<td>April 8, 1992</td>
<td>Raj Kumar Ranbir Singh (CM)</td>
<td>a minority after 7 legislators, including 2 ministers withdrew support thereby</td>
<td>by R.K. Ranbir Singh was reduced to a</td>
</tr>
<tr>
<td></td>
<td>Manipur People's Party</td>
<td>reducing the strength of the ULF to 24 in the 60 member Assembly. However, the</td>
<td>minority after 7 legislators, including 2</td>
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<td>Speaker created a constitutional crisis by disqualifying the Opposition members</td>
<td>ministers withdrew support thereby reducing</td>
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<td>(defectors) whenever a no-confidence vote against the Ranbir Singh government</td>
<td>the strength of the ULF to 24 in the 60</td>
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<td>came up in the Assembly. The Supreme Court set aside such disqualifications, but</td>
<td>member Assembly. However, the Speaker created</td>
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<td>the Speaker for collateral and mala fide reasons did not allow them to vote. This</td>
<td>a constitutional crisis by disqualifying the</td>
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<td>drama led to President’s Rule. The Assembly was kept suspended.</td>
<td>Opposition members (defectors) whenever a</td>
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<td>no-confidence vote against the Ranbir Singh</td>
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<tr>
<td>December 15, 1992 to</td>
<td>Himachal Pradesh:</td>
<td>Because of the demolition of the disputed Babri Masjid structure in Ayodhya. The</td>
<td>Because of the demolition of the disputed</td>
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<tr>
<td>December 1993</td>
<td>Shanta Kumar (CM) Bhartiya Janata Party (BJP)</td>
<td>Governments in these states were</td>
<td>Babri Masjid structure in Ayodhya. The</td>
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<td>Madhya Pradesh:</td>
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<td>Governments in these states were</td>
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<td></td>
<td>(Sunderlal Patwa)</td>
<td></td>
<td>S.R. Bommai v. Union of India [ AIR 1994 SC 1918]</td>
</tr>
<tr>
<td>State</td>
<td>Party &amp; Leader</td>
<td>Reason for President's rule imposition</td>
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<tr>
<td>Rajasthan</td>
<td>Bhairon Singh Shekhawat</td>
<td>Government headed by Kalyan Singh failed to perform its Constitutional responsibilities.</td>
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<tr>
<td>Uttar Pradesh</td>
<td>Kalyan Singh</td>
<td>Silent witness to the anarchy and disorder unleashed in Ayodhya.</td>
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<tr>
<td>Tamil Nadu</td>
<td>Kalaignar Muthuvel Karunanidhi</td>
<td>President's rule was imposed on the ground of breakdown of law.</td>
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Application of the Emergency Provisions since 1985
<table>
<thead>
<tr>
<th>April 6, 1991 to June 23, 1991</th>
<th>Haryana: Om Prakash Chautala (CM) Janata Dal</th>
<th>Article 356(1)</th>
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<td>and order situation as well as failure of Constitutional machinery in the State. Reportedly, the State Government was charged with encouraging the violent activities of LTTE, and the United Liberation Front of Assam (ULFA). It is to be noted that for quite some time the AIADMK and the Congress(I) were demanding the dismissal of the Karunaidhi government. Hence Chandra Shekhar advised the President accordingly. The Janata Dal ministry was reduced to a minority, following the disqualification of 3 legislators by the Speaker under the Anti-Defection law. The CM recommended the dissolution of the Assembly, but the Governor called upon him to prove his majority in the Assembly. Chautala challenged the right of the Governor to</td>
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<td>Date</td>
<td>Location</td>
<td>Article</td>
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prove his majority. But finally the imposition of President’s rule was recommended by the Governor.

The B.B. Lyngdoh ministry, which enjoyed the majority support was dismissed, in complete disregard of the Supreme Court’s order. Actually the Assembly was summoned in August, to discuss the vote of confidence in the Ministry, where 30 members voted for it and 20 against it. Before announcing the result, the Speaker declared that 5 members, who voted for the motion was disqualified. The Supreme Court had ordered that the support of 4 independent members (who were disqualified), should be counted. The Speaker allowed them to vote but did not count them, and exercised his casting vote declaring the motion lost. When the CM did not
| October 10, 1990 to October 17, 1990 | Karnataka: Veerendra Patil (CM) Indian National Congress (INC) | Political crisis arose in Karnataka after Rajiv Gandhi publicly announced that Veerendra Patil has been asked to step down, in view of his bad health and incapacity to deal with the communal situation. Patil refused to quit. Meanwhile the Congress legislature party elected a new leader. The Governor decided to side with Patil and ignore the decision of the party, as he thought it was illegal and against the party's constitution. Patil claimed that he had majority support and recommended the dissolution of the Assembly. However, The Governor recommended the imposition of the President's rule for a |
### Application of the Emergency Provisions since 1985

<table>
<thead>
<tr>
<th>Date</th>
<th>Region/Party</th>
<th>Article</th>
<th>Reason for Application</th>
</tr>
</thead>
<tbody>
<tr>
<td>July 18, 1990 to October 9, 1996</td>
<td>Jammu &amp; Kashmir Farooq Abdullah (CM) National Conference (NC)</td>
<td>Article 356(1)</td>
<td>Governor’s rule was imposed under section 92 of the J&amp;K Constitution after the resignation of the National Conference – Congress (I) coalition government headed by Farooq Abdullah, in protest against the appointment of Jag Mohan as the Governor of the State. Since under J&amp;K’s Constitution, Governor’s rule cannot be extended beyond 6 months, President’s rule was recommended by the Governor, because of the terrorist activities which deteriorated security and political situation in the State.</td>
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<tr>
<td>December 14, 1990 to January 25, 1991</td>
<td>Goa: Luis Proto Barbosa Indian National Congress (INC)</td>
<td>Article 356(1)</td>
<td>President’s Rule was imposed after a series of political developments that resulted in a situation in which no group was able to establish majority in the Assembly. On December 4, 1990,</td>
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</table>
Maharashtra Party (MGP) withdrew its support to the Progressive Democratic Front (PDF) Government and thereupon on December 6, 1990, a notification was issued summoning the Assembly on December 10, 1990 and Dr. Barbosa, was required to seek a vote of Confidence. Before the Assembly could meet Dr. Barbosa tendered his resignation as the Chief Minister on December 10, 1990 and the same was accepted. On December 10, 1990, Dr. Wilford D'Souza, leader of the Congress (I) Legislature party staked his claim to form the Government. He claimed the support of 20 Members consisting of 13 Members of the Congress (I), 4 Members of Goa People's Party (GPP) and 2 members of MGP, who would form a common front known as the
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<tr>
<th>Event</th>
<th>Parties Involved</th>
<th>Provisions Referenced</th>
<th>Case Cited</th>
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<tbody>
<tr>
<td>November 27, 1990 to</td>
<td>Assam: Prafulla Kumar Mahanta (CM) Asom Gana Parishad (AGP)</td>
<td>Article 356(1)</td>
<td>In Assam President's Rule was imposed on 29 November 1990 on the ground that free and fair election was not possible due to the deteriorating law and order situation arising out of activities of the United Liberation Front of Assam (ULFA). The Assembly was put under suspended animation. The Peoples Union for Human Rights (represented by Ramesh Kumar Jain and Ors.) V. Union of India (UOI) and Ors. [AIR1992Gau23]</td>
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<tr>
<td>June 30, 1991</td>
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<td>Date</td>
<td>Location</td>
<td>Party</td>
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<td>April 21, 1989 to November 30, 1989</td>
<td>Karnataka: Somappa Royappa Bommai (CM) Janata Dal</td>
<td>Article 356(1)</td>
<td>The reason for imposition of the President's Rule is that Sri. S.R. Bommai had lost the majority support in the House (because a number of members defected from the party) and no other party was in a position to form the government. After the series of defection, the CM, however reported to the Governor that he was prepared to prove his majority on the floor of the Legislature. But the Governor did not agree and sent his report to the President, without</td>
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*S.R. Bommai v. Union of India [AIR 1994 SC 1918]*
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<tr>
<th>Date</th>
<th>State</th>
<th>Leader</th>
<th>Event Description</th>
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<tr>
<td>January 30, 1988 to</td>
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<tr>
<td>January 27, 1989</td>
<td>Tamil Nadu:</td>
<td>Janaki Ramachandran</td>
<td>After the death of M.G. Ramachandran, the Governor called upon his wife Janaki Ramachandran to form a government on the condition that she must secure a vote of confidence within 3 weeks. The trial of strength took place on 28 January 1988. On that day the legislators indulged in violence and the police had to be called to restore order. In this situation the Governor reported to the President that Janaki Ramachandran was leading a minority government. The Governor’s report was also critical of the Speaker’s role in adjourning the House on frivolous grounds. The report also underlined that horse-trading had also taken place before the actual consideration of the confidence motion.</td>
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<td>AIADMK</td>
<td></td>
<td>(CM)</td>
<td>even exploring the possibility of an alternative government.</td>
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<td>September</td>
<td>Mizoram:</td>
<td>Article</td>
<td>A split within the</td>
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<td>Date</td>
<td>Region/Party</td>
<td>Article</td>
<td>Description</td>
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<tr>
<td>7, 1988 to</td>
<td>Laldenga(CM)</td>
<td>356(1)</td>
<td>Ruling Mizo National Front (MNF) reduced Chief Minister Laldenga's faction to a minority in the State Assembly. 8 of the MNF's 25 legislators formed a new party called the Mizo National Front (Democratic). The split occurred over Laldenga's unilateral suspension of two party members. The Congress (I) chief Lanthanwala staked his claim to form a coalition government, with the help of the breakaway group. However, the Speaker created a constitutional crisis by suspending 8 of these members during the pendency of proceedings for their disqualification. Hence Rajiv Gandhi declared President's Rule in Mizoram.</td>
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<td>January 24,</td>
<td>Mizo National Front – (Mizoram</td>
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<td>1988</td>
<td>regionalist)</td>
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<tr>
<td>June 19,</td>
<td>Haryana: Bansi Lal (CM)</td>
<td>Article</td>
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<tr>
<td>1987 to July</td>
<td>Janata Dal</td>
<td>356(1)</td>
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<td>7 1987</td>
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<td>May 11,</td>
<td>Punjab: Surjit Singh Barnala (CM)</td>
<td>Article</td>
<td>After the Rajiv-Longowal agreement, an election was held in Punjab and an Akali Dal</td>
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<td>February 23,</td>
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<td>1992</td>
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government was formed under Surjit Singh Barnala. The violence and terrorism that plagued Punjab escalated, and there was a complete breakdown of law and order. The Governor’s report stated that the law and order situation deteriorated, and that the situation was further aggravated by the fact that the ministers had close links with the terrorists. Hence President’s rule was imposed, but the legislature was kept in suspended animation in the hope that the government could be revived if the situation improved. In May 1988 the Punjab police and Indian paramilitary forces launched Operation Black Thunder against armed extremists who had again created a fortified stronghold within the Golden Temple. At least 40 extremists and several police officers were killed.
| September 7, 1986 to November 6, 1986 | Jammu and Kashmir:  
  Ghulam Mohammad Shah (CM)  
  Awami National Conference | Article 356(1)  
  The twenty months old G.M. Shaw ministry fell when the Congress (I) withdrew its support. As no alternative Government was feasible, the Governor’s rule was proclaimed under section 92 of the J&K Constitution, on 7th March 1986. The Assembly was kept under suspended animation, but all the opposition parties soon demanded that the Assembly should be dissolved and fresh elections should be held and Farooq Abdullah even threatened that 34 members from his party will resign. Under sec 92, the promulgation was operative only upto 6th September. So the Governor reported to the President that the... |
|   |   | security of the state was under threat and that the composition and the strength of the political parties were such that political instability would continue. Hence the President's Rule was imposed. |   |
Summary of the presentation by panellists on the workshop on “The Nature of Indian Federalism”

Panelists and Chairs of sessions:
Mrs. Justice Ruma Pal
Prof. (Dr.) Mahendra Pal Singh, Vice Chancellor The W.B. National University of Juridical Sciences
Mr. Justice S. Ravindra Bhat, Delhi High Court
Prof. (Dr.) Harihara Bhattacharya, Burdwan University
Prof. (Dr.) Mahendra Prasad Singh, Delhi University
Dr. Rekha Saxena, Delhi University
Prof. (Dr.) Sudhir Krishnaswamy The W.B. National University of Juridical Sciences

A workshop themed *The Nature of Indian Federalism* was organized at The West Bengal National University of Juridical Sciences on August 2nd, 2009, wherein some of the leading scholars, members of the bar, and the bench discussed and analyzed various aspects of Centre-State relations in India. The main purpose for the workshop was to seek further views from experts in this area, so that before submitting the final draft report to the Commission on ‘Centre-State Relationships’, the researchers are able to add, modify, and enrich their analysis.

The first speaker for the day was Prof. Harihara Bhattacharya, who spoke on *Globalization and Indian Federalism: Paradigmatic Shifts*. The main focus of his discussion was to trace the contextual changes in Federalism in the last decade. He began by stating that the history of Federalism co-existed and survived through three kinds of paradigms - Liberalism, Social-Welfarism and Socialism. But the Socialistic paradigm was inhospitable to federalism mainly because it failed to develop the civic national identity, which is based on ethno-regional and ethno-linguistic identity, which is essential for federalism. Also, initially the welfare state, being highly bureaucratic and centralized, was not hospitable to federalism, but it later somehow adapted itself into it. According to the Professor Bhattacharaya, one of the strengths of a combination of welfare state and federalism
especially in multiethnic countries is that it provides for a social policy that helps in mitigating ethno regional conflicts so as to lessen political cleavages.

Then he moved onto the shifts in paradigm, saying that in one graphic phase, it is understood as a kind of change from a world of sovereign nation states to a world of diminished state sovereignty, which is considered congenial for resurgence of federalism. Certain distinctive features of this new global reality, in the post-sovereignty era was then pointed out. The first one being the recognition of more and more decentralized forms of governance, and the second is the recognition of diversity and difference. He also mentioned the connecting factors between recognition of difference and globalization and then moves onto the third feature which is that the globalizing world is emphasizing on cosmopolitanism and multiple spheres of governance, shifting allegiances, new forms of identity and overlapping jurisdictions. It is according to these contexts that federalism has to be redefined.

Then he moved on to Indian scenario especially focusing on the changes that took place post 1990's, when globalization was openly embraced in India.

The second speaker for the day was Professor (Dr.) Mahendra Prasad Singh who spoke on the Amendatory, Legislative, and Judicial Effects on Union-State Relations with Special Reference to the Seventh Schedule of the Constitution.

He began his presentation by explaining the dualist and integrated models of distribution of powers in federal states. Highlighting the essential characteristics of the models, the need for an institutional mechanism for the functioning of different units of federation was established. A mapping of exercise of the institutional mechanism of the federations of the world was further done to place and understand the configuration of distribution of power in India.

Professor Singh then identified the amendments in Seventh Schedule as done in eight lots and then proceeded to evaluate its impact. A pattern of consistent transfer of subjects from State List to Concurrent and Union lists through amendments was illustrated to argue that the amendments in Seventh Schedule resulted in magnifying the powers of the Union.

According to Professor Singh, centralisation of powers, is evident and is a continuation from Nehurvian period. The one way traffic of usurpation of power though evident has
neither became a matter of political debate nor consistently challenged in a court of law. It was pointed out that the trend of centralisation is continuing as if there is a national consensus. The party system, public policy regime and the national character of the political leadership were identified as contributory factors.

Then the Professor moved on to identify, the ways in which the Centre can increase its control over States, despite the demarcation of subjects matter in Seventh Schedule. It was mentioned that Centre sponsored schemes, Central expenditure on the State subjects and the potential of Central legislation to elbow out State’s role were avenues of centre to increase its control over State. Channelization of allocation and programmes through Planning Commission, the role of the states in Planning Commission, the structure and functioning of Empowered Group of Ministers and fiscal institutions were also critically examined to appraise the working of Seventh Schedule.

Dr. Rekha Saxena was the next speaker for the day, who spoke about the Impact of Judiciary and Legislative Acts on Intergovernmental Interactions in the Indian Federal System. The main theme of the discussion was the impact of globalisation on Sub National Governance and the resultant effect on inter-governmental relation, which in turn affects the federal system.

Dr. Saxena, identified the growing jurisdictional conflicts as a feature of present intergovernmental relations. It was mentioned that independent regulatory authorities and direct dealings of stake-holders with regulatory bodies contribute to the tensions in executive federalism.

The impact of globalisation on federal system was also assessed in this presentation. It was pointed out that while on one hand the states are benefitting from globalisation, it is also true that on the other hand it results in the creation of forward and backward States; States gaining and not gaining from globalisation. According to Dr. Saxena, the growing trend of federalisation, and gaining importance of provincial leaders as well coalition building at the centre, foreign relations should be conducted on a more broad-based consensus between the Centre and the States. Highlighting the dynamics of the working of WTO and the emerged globalised market economy, it was argued that in the changed circumstances, the Union Government should develop effective mechanisms for coordination while exercising its treaty making and policy making functions. The need for institutionalisation of such mechanism was also emphasized.
In the third session for the day, **Professor (Dr.) Sudhir Krishnaswamy**, spoke about *Multi Layered Government under the Indian Constitution*. He primarily referred to a string of cases which communicate significantly about the nature of evolving Indian Government. He began by focusing on three cross-cutting themes that are endemic to any discussion on Local Government. These being, whether the local governments are recreations of indigenous institutions or are they new modern institutions; whether this is federalism extended or is it a truly multi-level government; whether the local government is essentially about democratic decentralization. One of the rationales behind local government is that apart from it being a good tool of political banishment, it also brings forth the idea of subsidiarity which prescribes an optimal organization between levels of government. The third reason, as mentioned is that it certainly acts as an efficiency device.

He then spoke on how these themes translate into cases, and he focused on three analytical categories of cases. The first category of cases which he points out is regarding the definition of local government, and the drawing of boundaries. The courts have been consistent in holding that in these matters the States have the prerogative and it can draw the Panchayats in any manner, for these are modern institutions, having no reference to traditional villages or indigenous communities. The second categories of cases are cases dealing with the conduct of elections. Here also the Courts have been consistent, and has been also willing to issue mandamus directing the States to hold elections, in case they are delayed. The third category of cases is those dealing with suspension and dissolution of Panchayats and municipalities. However the Courts have not discussed on this point adequately and have failed to address the issue of constitutional compliance.

Subsequently he focussed on the powers and functions of the local governments, where it was pointed that though they have no lawmaking function, they do have a strong scrutinizing function. Hence primarily the conflicts which arise are executive level conflicts. The executive functions enumerated in the Schedules, are so broadly framed that they automatically overlap with the State's executive functions, but conflicts are avoided by the device of delegation. However, two very important cases were pointed out, - *Smt. T.J. Manjamma W/o S. Yoga and Ors. etc. etc. v. State of Karnataka, etc.*\(^{205}\) and *Ranga Reddy District Sarpanches’ Association and Ors. v. Government of A.P. and Ors*\(^{206}\) where the State initially delegates the power to the Panchayats and municipalities, but later it wants to act on it. In both the two cases the State’s order was struck down. However there are other High Court cases where it was held otherwise.
With respect to fiscal distribution, it was said that the State Finance Commissions must evolve a formula for deviation of funds between the Panchayats and State Government. Also a reference was made to the Gram Nyayalayas Bill, 2008, and the debate regarding whether they are a part of informal community justice or another tier of the formal court system.

It was then suggested that some new conflict rules are required to deal with the conflicts between the local government on one hand and the State Government and the Union Government. The question of direct transfers has also been briefly dealt with in the question answer session.

Prof. Krishnaswamy, also mentioned that there can be two kinds of executive conflicts regarding overlapping jurisdictions and over-stepping jurisdictions. There has been an evolving practice, where heads of local government are brought into the committee or commission structure and into a conflict resolution model. But it was suggested, that even the political model has to be either three-part commissions where the Union, State and the local governments sit together, or some sort of enforced public mediation structure has to be evolved, thereby avoiding court based resolution and advancing a model for the three-part complex structure.

After this there was a question-answer session, where many points regarding Panchayat conflicts, devolution of powers, Gram Nyayalayas Bill, 2008, the role of the centre in granting money directly to the panchayats, and various aspects of 73rd and 74th Amendment was discussed.

The last speaker for the day was Mr. Justice Ravindra Bhat, who spoke about Potential Areas for Reforms. He mainly confined his discussion to one specific area, which is Inter-State water disputes, the problems associated with it and advocated that since Inter-State river is a national resource, it should be centralized i.e., there is a requirement of setting up of a regulatory body which will also look into the regional and local concerns and also the environmental concerns, as long as allocation doesn’t happen.

The problems regarding the present machinery for resolving the Inter-State river disputes are that it is very time consuming; secondly, problems are solved based on only legal and constitutional principles. It also brings to a standstill the developments within the basin, and forestalls inter-basin transfers. The existing mechanisms also tend to over-look the environmental concerns. The environmental impact is noticed only much later. Hence
the local communities concerns over flooding, catchments areas being deprived etc do not get voiced in the Inter-state river tribunals.

It was pointed out that the inspite of the Doctrine of Equitable Apportionment being followed by the Courts as early as 1960’s, the States continue to claim riparian rights or prior user rights. According to Justice Bhat, this area needs to be legislated upon. There should be a restatement of the doctrine through a common legislation involving Entry 56, List I.

Maximization of water utilization and allocation to people should be the first objective which is required to be achieved. There should be a people-oriented approach, rather than the claims being made only by the States, and hence a need to encourage Inter-State and Intra-State river valley planning.

The second requirement is to devise a mechanism about data collection about rain, soil, crop patterns, industrial and domestic use and even energy, i.e. data collection machinery or a data collection bank is required for they help in incentivizing quick, objective assessment of water needs of people. The possibility of enacting presumptive provisions to data collected by independent effort could shorten the litigation time. Also a master plan is required to devise mechanisms for irrigation, distribution of power etc. within the basin states and address environmental concerns rather than facing environmental challenges later.

With respect to the solutions pointed out, the first of them was taking a close look at the mechanisms supporting compact between the States, which is prevalent in Australia. Exploring the possibilities for a statutory nation-wide commission or authority independent of daily political pressures comprising of a federated structure incorporating river basin authorities and water user associations and fixing the time periods for negations and adjudications could be other solutions. The above will help in arriving at quicker solutions to Inter-State water disputes. It was also stated that the existing model may be retained in the sense that the ultimate adjudicatory power may be left with the Courts, but the primary decision is to be left with some sort of political technical expert agency.

Lastly it was mentioned that the existing model is such that even when binding decrees are given by the Courts, they are not implemented in a proper manner. Therefore, there is definitely a need to devise new mechanisms for resolving Inter-State water disputes.

This was followed by a question answer session, followed by a vote of thanks.
Working of Coalition Governments in Comparative Perspective

By

Mahendra Prasad Singh

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University of Delhi
Delhi 110007

Delhi
October 2009
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Working of Coalition Governments in Comparative Perspective

Introduction

Coalition formation is inherent in organized politics. It is also a legitimate political activity in a democracy. It is difficult to imagine political parties or parliaments that can do without coalition formation of some kind or the other. However, the objective of my proposed research is to study the functioning of coalition governments in a comparative perspective, not coalition politics per se. In other words, this report examines the phenomenon of *inter-party* rather than *intra-party* coalitions for formation and maintenance of governments in (a) parliamentary or parliamentary-federal constitutional contexts, and (b) recourse to presidential-congressional coalitions for bridging the gulf created by separation of powers among governmental organs in the United States-type presidential or presidential-federal systems.

A coalition situation in a parliamentary setting arises when an election fails to throw up a party with a majority of seats in a parliament and no single party is able to form a government according to the majority decision rule for government formation and maintenance in conformity with the confidence convention of parliamentary government, with the confidence vote tied to the popularly elected house of the Parliament. What is said above is applicable to parliamentary-federal as well as semi-presidential systems that seek to combine presidentialism with parliamentarism as in France, Sri Lanka, and Russia with some variations. Only, the U.S.-type presidential system requires a discussion of executive-legislative coalitions with a different conceptual framework from the one used in parliamentary governments with confidence requirement.

Another caveat is in order here. Coalition as an ubiquitous political activity also occurs among political parties and groups at electoral level, and there is some degree of connectivity between the electoral, parliamentary, and executive planes. Electoral coalitions are beyond the scope of the present study and report.
The discussion in what follows is organized into the following sections. Part II reviews the major theories of coalition behaviour in the political science literature. Some of these theories, especially those operationalized at micro-level with the assumptions of methodological individualism, are too abstract and trapped in mathematical model-building to be of much relevance in a study of coalition-behaviour at the macro-level. Application of theories in this study is also dependent on availability of quantitative and comparable data on a cross-national basis. Part III discusses coalition governments in the Commonwealth parliamentary and parliamentary-federal systems. Part III analyses the subject in the West European parliamentary and parliamentary-federal governments. Part IV is addressed to the examination of coalition governments in some Asian parliamentary or parliamentary-federal systems. Part V is concerned with the experience of coalition governments in presidential-federal and semi-presidential political systems. Finally, Part VI offers the concluding remarks meant to serve as an executive summary with policy or reformist implications.

Part I

Theories of Coalition Behaviour

Theories of political coalitions may be classified into four broad types. First, there are theorizations that focus on causes of coalition government that go beyond the symptomatic condition of a hung Parliament (without a majority party). The search of causes may be found in the sociological as well as political factors. Sociological causal theories postulate that, all other factors being the same, a country with greater cultural and social diversities may be expected to be more likely to have coalition governments than one which is relatively more homogeneous. The latter are less likely to be deeply divided and can thus be more amenable to political aggregation and democratic governance. To say it is not, however, to assert that democratic consensus is an impossible proposition in countries with deep and abiding cultural and social cleavages.

John Stuart Mill (1972: 228), conceptualizes “representative government” as one in which “the whole people, or some numerous portion of them, exercise through deputies periodically elected by themselves the ultimate controlling power, which in every constitution must reside somewhere. This ultimate power they must possess in all its completeness. They must be masters, whenever they please, of all the operations of
government”. Then he goes on to make the telling statement: “The power of final control is as essentially single, in a mixed and balanced government, as in a pure monarchy or democracy”. Mill’s conception of the “people” here is as singular as Thomas Hobbes’s conception of the absolute monarch. Coalitional solutions spring from a more pluralistic conception of the people. Ironically, in a subsequent phase of democratic theory particular interests came to be conceptualized but they were again merged with a more generalized and abstract notion of interest and its representation in government. In such a conception, “a representative”, remarks Norberto Bobbio (1987: 48), “means a person with two very specific attributes: someone who (a) enjoys the trust of the electorate by virtue of election and so is responsible to them and therefore cannot be dismissed; and (b) who is not directly answerable to the electorate precisely because he is called upon to safeguard the general interests of civil society and not the particular interests of any one group”.

More patently political causal theories bearing on coalition government focus on electoral laws and nature of the constitution. Maurice Duverger (1963) and William Riker (1982) separately professed to have discovered an “iron-law” that plurality or first-past-the-post electoral system produces a two-party system, whereas proportional representation leads to a multi-party system. And it goes without saying that coalition governments are more strongly correlated with multi-party systems than with two-party systems where one-party majority governments are supposed to be the norm.

By now we know, however, that the supposed universal law of Duverger and Riker is only probabilistically or statistically true. For the more recent experiences of Canada and India suggest that even plurality electoral law can possibly yield coalition and/or minority governments. However, the Duverger-Riker law may still be contextually valid, if not universally. For in culturally and socially homogeneous settings, in relative terms, plurality electoral system does more often than not produce party systems that are, formally by and large bi-partisan. But in countries characterized by deeper diversities neither the homogenizing effects of plurality electoral law nor those of the parliamentary system (government-opposition bi-polarization) are sufficient to necessarily engender a two-party system. Proportional representation elections and federal political systems, of course, set in motion strong political forces causing coalition governments. In other words, the original relationship between plurality electoral system and party system is intermediated by a “third” factor, namely, socio-cultural and regional diversity which confounds the predicted outcome.
The impact of the form of the constitution on majority, minority, or coalition government is also inter-mediated by the party system. A parliamentary government tends to encourage a two-party system, or at any rate a bi-coalitional pattern, by demanding government-opposition polarization in the parliament. And, it goes without saying that coalition/minority governments are typically a feature of multi-party systems. A federal government – either within parliamentary or presidential setting – encourages multiplicity of parties by creating at least one more domain of party politics, i.e. the regional governments. Most federal systems end up having more regional parties in addition to the national ones than a parliamentary system. This makes coalition/minority governments more likely in federal and federal-parliamentary systems than in purely parliamentary systems.

A second set of coalition theories are utility maximization theories that postulate the size principle that predict the minimum winning coalition. Proceeding from the axiom of the rationality of political actors, these theories deduce the theorem that in any formal coalition situation with the majority decision rule the coalition formation would hover around the minimum winning size, typically around 50 + percentage points. The smaller the coalition, the larger the quantum of power and patronage to be shared among the winners (Gamson 1961; Ricker 1962).

Third, there are ideological and policy compatibility theories. Proceeding from the assumption that the maximization of utility must contend with ideological concordance among parties, these theories predict a minimum winning coalition among parties whose policy preferences are least discordant. (Axelrod 1970; De Swaan 1973).

Fourth, there are theories that treat coalitions as sequential episodes that offer opportunities for redistribution of political resources that determine the relative political influence of coalition partners. The gains and losses in the present round and their implications for ensuing ones primarily guide the competitive demands and concessions made by parties to each other (De Mesquita 1976; Iorio 2007).

The Fifth set of theories deal with the supposed various effects of coalition governments on politics and economy. In the political domain coalition government is supposed to be conducive to consensual or consociational policy making and governance, though indecisiveness and delays are considered negative effects. Federal coalition governments are particularly a standard power-sharing mechanism likely to promote national
integration. Coalition governments are commonly unpopular with business and industries circles, but once political conflicts engendered by majoritarian government linger and adversely affect the economy, the perceptions often change.

Part II

Commonwealth Parliamentary and Parliamentary-Federal Systems

This class of political systems in this study includes the United Kingdom, Canada, Australia, New Zealand, India, Malaysia, and South Africa, among others. The cases selected here for analysis in relation to coalition government range from highly developed countries in economic and political terms (the UK, Canada, Australia, and New Zealand) to fairly developed (India and Malaysia) and developing ones (South Africa). Applying an interesting typology of seven patterns of political modernization formulated by C.E. Black (1966/1967: chapters 3 and 4) here, we find that Great Britain belongs to the first pattern (with the only other contender, France) where consolidation of modernizing leadership took place between (1649-1832), modernizing economic and social transformation occurred during 1832-1945, and integration of society may be said to have been achieved by 1945. Canada, Australia, and New Zealand form part of the second pattern (with only other contender, the United States of America) where the three foregoing corresponding analytical tasks of political modernization were accomplished between 1791 to 1907. India, Malaysia, and South Africa are categorized with the sixth pattern comprising, at Black's writing in the mid-1960s, 34 independent and 29 dependent societies “with a population of about 1 billion, the traditional cultures of which are sufficiently well developed that they could interact with those of the more modern tutelary societies in their adaptation to modern functions” (Black 1966: 123-24). In Black's opinion the consolidation of modernizing leadership in South Africa occurred between 1910-1962 and in India between 1919-1947, and in Malaysia it started in 1963. He dates significant economic and social transformation in India back to 1947 and in South Africa to 1962. One may differ from Black's assertion about South Africa's socio-economic transformation as the racial policy of apartheid (euphemistically called “separate development” in official circles) continued through most of the 20th century. Racial policies were gradually eased during the 1970s and 1980s, but the division of the population into four racial or ethnic communities has continued: Blacks (75.2 per cent), Whites (13.6 per cent), Cape Coloureds (8.6 per cent), and Asians (2.6 per cent) (According to the 1998 estimates).
An overview of cultural cleavages in the category of political systems under study here in the context of sociological bases of coalition governments is presented in Table 1. The three indicators of cultural difference used here are religion, language, and ethnicity. The data presented here show that these countries are not exactly monolithic, yet they are not extremely fragmented. These polities, for all practical purposes, range from being conglomerate to moderately diverse, with India and South Africa partly included and partly excepted. The numbers of religious groups with 1 per cent+ in the total population range from three in the United Kingdom and Australia to six in Canada. The corresponding data are five in South Africa, four each in India and New Zealand, and three in Australia. However, the dominant religious in these countries are Christianity (Britain, Canada, Australia, New Zealand, and South Africa) Hinduism (India) and Islam (Malaysia). This dominance ranges from 88.7 per cent of Muslims in Malaysia and 57 per cent of Christians in New Zealand. India, to be sure, had suffered a partition by the British colonial rulers on religious basis in 1947 and is still afflicted by religious conflicts. But the country may be said to have managed its denominational politics reasonably well through multicultural secularism and federal democratic politics.

Table 1

Major Cultural Cleavages in the Selected British Commonwealth Political Systems (% in Total Population)

<table>
<thead>
<tr>
<th>Countries</th>
<th>No. of Religious Groups (1%+)</th>
<th>No. of Linguistic Groups (1%+)</th>
<th>No. of Ethnic Groups (1%+)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Britain (Population 49,138,831 in 2001)</td>
<td>3 (71.60% Christian, 2.7% Muslim)</td>
<td>1 (English de facto national language)</td>
<td>5 (92.1% White, 2% Black)</td>
</tr>
<tr>
<td>Canada (Population 31,612,895 in 2006)</td>
<td>6 (72.8% Christian, 2% Muslim)</td>
<td>2 (75% English, 25% French)</td>
<td>14 (32.22% “Canadian” by response, 21% English)</td>
</tr>
<tr>
<td>Country</td>
<td>Population</td>
<td>%Christian</td>
<td>%Muslim</td>
</tr>
<tr>
<td>------------------</td>
<td>--------------------------</td>
<td>------------</td>
<td>---------</td>
</tr>
<tr>
<td>Australia</td>
<td>21,262,641 in 2009</td>
<td>63.8%</td>
<td>2.1%</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>New Zealand</td>
<td>4,143,279 in 2006</td>
<td>57%</td>
<td>2%</td>
</tr>
<tr>
<td>India</td>
<td>1.17 billion in 2009</td>
<td>80.5%</td>
<td>13.4%</td>
</tr>
<tr>
<td>Malaysia</td>
<td>27,730,000 in 2008</td>
<td>88.7%</td>
<td>8.9%</td>
</tr>
<tr>
<td>South Africa</td>
<td>47,850,700 in 2007</td>
<td>79.7%</td>
<td>1.5%</td>
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**NOTE:** The Indian census do not use the category of ethnicity, but caste and tribe and _varna_ may be the Indian equivalents. No _varna_ census has ever been conducted, the last caste census was held in 1931, and presently only Scheduled Castes (SCs) (former untouchables) and Scheduled Tribes (STs) (also called _janajatis_ or _adivasis_) are enumerated for implementation of reservation policies. In 2001 SC population was 16 per cent and ST proportion in the total population was 8 per cent.
The pattern of cultural cleavage in religious terms in these polities more or less replicates on linguistic and ethnic dimensions. Britain and Australia are virtually unilingual countries where English is de facto national language. New Zealand census report seven languages spoken by sections of population forming 1 per cent or more of the people, yet English speaking population is solidly 98 per cent. Malaysia is predominantly Malay in linguistic term, followed by Chinese dialects and Indian languages. English is also widely used and is a compulsory subject in primary and secondary schools in Malaysia. Canada is linguistically bicultural (75 per cent English and 25 per cent French), though the country since the early 1970s has proclaimed multiculturalism as the official policy of the federal government. The French are largely concentrated in the province of Quebec and partly in New Brunswick, though the federal government scrupulously follows a bilingual official language policy. Quebec separatism surfaced significantly since the 1970s but the country seems to have turned the corner on separatism by a vigorous pursuit of asymmetrical federalism. India and South Africa are exceptionally diverse in linguistic terms, with 12 linguistic groups accounting for 1 per cent or more of the population in India and with 11 official languages in South Africa. The number of official languages of the Union government in India are two – Hindi and English, with various state governments officially using their regional languages or English. Yet Hindi and English are the lingua franca of India and South Africa even though numerically it is the fifth language in the latter as is estimated to be spoken by only 2 per cent of the population in the former.

On ethnic dimension the dominant ethnic groups in the United Kingdom are the Whites (92.1 per cent), and in South Africa the Blacks (75.2 per cent). Europeans constitute 73 per cent of the population in New Zealand. In Canada and Australia interestingly the largest segments of populations in response to the question relating to ethnicity in census enumerations self-styled themselves as “Canadians” (32.22 per cent) and “Australians” (37.13 per cent), respectively.

The foregoing pattern of cultural cleavages in the selected polities of the Commonwealth would, going by available theories as well as conventional wisdom, prompt one to intuitively expect majority governments in the White countries of the group and coalition governments in India and South Africa. This expectation is only partly met in the cases concerned, as is discussed in a subsequent section. In brief, the White Commonwealth polities are more likely than not to have one-party majority governments, especially historically. But in more recent contemporary times this trend has come under pressure in the United Kingdom, occasionally breached in Canada and Australia, and
perhaps irreversibly altered in New Zealand. In Brown and Black Commonwealth India and South Africa there have either been one-party dominant governments due to special historical circumstances of the national liberation movements and their hangovers or belatedly multi-party coalition/minority governments in India. South Africa may also follow India’s political trajectory when the dominance of the African National Congress, like that of the Indian National Congress, declines in coming decades. Malaysia has been a quasi-democratic dominant party system with coalition in government as well as on the opposition side at the national level.

Now, we turn to political causal factors bearing on coalition governments in the Commonwealth political systems. We will examine here the impact of three institutional variables in this context, i.e. the system of representation, parliamentary form of government, and parliamentary-federal form of government. These variables in relation to the cases examined here are presented in Table 2. All these countries, excepting New Zealand and South Africa follow variants of the plurality or first-past-the post (FPTP) electoral system for parliament's popular chamber elections. Even New Zealand followed this system from 1914 to 1996, when it switched over to proportional representation to avoid electoral distortion of the winning party getting more seats even though the runner-up got more votes, as in 1978 and 1981 when the National Party got more seats while the Labour Party registered more votes. Following a Royal Commission Report (1986)

Table 2
Form of Government and Systems of Representation in the Commonwealth Polities

<table>
<thead>
<tr>
<th>Systems of Representation</th>
<th>Forms of Governments</th>
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<tbody>
<tr>
<td></td>
<td>Parliamentary</td>
</tr>
<tr>
<td>Plurality</td>
<td>Britain New Zealand (Pre-1996)</td>
</tr>
<tr>
<td>Proportional</td>
<td>New Zealand (Post-1996)</td>
</tr>
</tbody>
</table>

**SOURCE:** Information on system of representation here and hereafter obtained from IDEA: International Initiative for Democracy and Electoral Assistance, [http://www.idea.int/esd/world.cfm](http://www.idea.int/esd/world.cfm), accessed on 21 September 2009.
recommending the adoption of mixed member proportional representation (MMP) and a non-binding referendum on electoral reforms in 1992, followed by a binding referendum in 1993, New Zealand adopted the MMP system. The first election under the new system was held in 1996. Australia from 1902 to 1983 held elections to the House of Representatives under the plurality electoral laws; in 1983 a modification was introduced which required the House elections to adopt alternative (“preferential” but not proportional) voting in response to the rise of the Country Party following the First World War and the consequent prospect of loss of seats to the Labour Party on account of the split of the non-Labour vote. The majority preferential variant on the plurality system has helped maintain the prominence of three major parties in the House of Representatives since then. The first democratic elections based on universal adult franchise were held in South Africa in 1994 under proportional electoral laws preparatory to constitution-making. The 1996 constitution adopted the list proportional representation for the national legislature.

Now, we proceed to discuss the type of party systems in the Commonwealth polities under review here. Reading tables 2 and 3 together, we find that the supposed impact of the representation system on the party system is most clearly borne out in the United Kingdom and New Zealand, though the former since the 1980s has partly deviated from the established pattern. The use of plurality electoral system in the UK through much of its history is strongly associated with a two-party system in that country, though a third major party, Liberal Democratic Party, has become systemically relevant since the 1980s, a trend that is sustained in the 2005 general election. New Zealand have had a de facto two-party system for nearly a century and a half, but it switched over to

<p>| Table 3 |</p>
<table>
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<tr>
<th>Party Systems with Majority/Minority/Coalition Government in Commonwealth Political Systems</th>
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<tbody>
<tr>
<td><strong>Country</strong></td>
</tr>
<tr>
<td>United Kingdom</td>
</tr>
<tr>
<td>Canada</td>
</tr>
<tr>
<td>Australia</td>
</tr>
</tbody>
</table>
mixed-member proportional representation in 1996 and overnight turned into a multi-party system with coalition governments. Plurality election system in Australia has not produced the same effect as clearly as in the foregoing two cases. Australia is a de facto two-party system, but with the complication that the second and the third parties have had a long-standing tradition of electoral as well as governmental coalition. The effect of plurality electoral law is diluted even more in Canada as its de facto two-party system have had to contend with a third party in the Parliament and a number of regional parties in several provinces. Since 1993 House of Commons election in Canada, the parliamentary party system there has become a multi-party affair. Canadians are averse to coalition governments but minority governments are not uncommon there. The hypothesized relationship between plurality representation and party system is flagrantly vitiated in India, where it produced one-party dominant system from 1952 to 1989 and a multi-party system with polarized pluralism since 1989 without a change of the electoral law. In a similar vein, the hypothesized relationship between proportional representation and party system is clearly negated by the South African instance where right since the first democratic elections in 1994 to date (September 2009) a one-party dominant system has prevailed with a mandatory coalition government in 1994 and voluntary coalition with the major opposition party since 1996. South Africa in all probability will follow the Indian political trajectory from a one-party dominance to a multi-party system in course of time.

Malaysia is quasi-democratic and quasi-federal, and its dominant party system has not developed into a truly competitive framework. It is rather “a hegemonic party system, centered on the dominant Barisan Nasional (National Front, BN) coalition, although the system does allow greater space for competition at the state level than would a comparable framework in a unitary state. In addition, democratic legitimacy is higher
for specific parties than for the competitive electoral authoritarian state as a whole, as contention is more vibrant and determinative within certain parties than between them” (Weiss 2009: 2). The 12th general election in Malaysia held in March 2008, however, may turn out to be a major democratic advance towards a competitive democratic and federal Malaysia. The National Front, BN, government of Prime Minister Abdullah Badawi based on a coalition made up of 14 national parties that had been in power since its formation in 1973 found its three-decade old two-thirds majority in the national parliament drastically reduced to a simple majority. The informal three-party opposition alliance quadrupled its parliamentary presence from 20 to 82 seats in the 222-seat Parliament. The Barisan Nasional coalition also suffered heavily at the state level losing control in four industrialized states of Penang, Perak, Kedah, and Selangor, while failing to dislodge the opposition government in Kelantan (Preston 2009; Singh 2009).

The United Kingdom began as a multi-party system, but since the 1920s the major parties were only two: the Conservative Party and the Labour Party, though a third party has always maintained a presence in the Parliament. The third party occasionally also played a role in delivering a working majority to one of the major parties forming the government. The two major parties in the nineteenth century were the Liberals and the Conservatives, but by the first decade of the 20th century Liberals were surpassed by the Labour. Since the mid-1970s a fourth party, the Social Democratic Party, also entered the House of Commons. In 1988 the Liberal Party and the Social Democratic Party merged to produce the Liberal Democratic Party, the third largest party presently. In addition, there are regional parties – called ‘Nationalist’ parties – in Scotland and Wales. The Scottish ‘Nationalists’ got a Scottish subparliament established under the Scotland Act (1998). Besides, there are some regional parties in Northern Ireland as well, including the largest pro-Belfast Agreement party, Sinn Fein. A major reform agenda of the Liberal Democrats is to replace the plurality electoral laws by some variant of proportional representation to address the disproportionate dominance of the Conservative Party and Labour Party. Coalition governments, typically called “national governments” have been formed in the U.K. to deal with national crisis like the Great Economic Depression of 1929-30s and wars. Great Britain was governed by multi-party coalitions during both world wars. Moreover, in hung Commons minority governments have also been formed with one or more opposition parties agreeing to bail out the government on votes on legislations and budgets. Nevertheless the hope that the historical bipartisan trend in Great Britain may,
after all, be restored dies hard. Pulzer (1976) believes that “a new election may reinstate a government, or series of governments, with a firm electoral base and a clear working majority, so that mid-seventies may slip into place as one of the adjustments, like those of the 1920’s and the 1980’s, that the system seems to need from time to time”.

Historically, party system in Canada may be seen as either a one-party dominant system in a short-range view or a de facto two-party system with a third party at the national level and several regional parties at the provincial level in a long-range view. The Conservative Party dominated party politics over much of the nineteenth century while the Liberal Party dominated for most of the twentieth. The 1993 House of Commons elections ushered Canada into a multi-party system of moderate pluralism. This pattern is maintained in the latest Commons elections in October 2008. Four systemically relevant parties continue to maintain appreciable parliamentary presence: Conservatives (vote share 37.65 per cent and seat share 46.4 per cent), Liberals (26.26 per cent and 25.0 per cent), Bloc Quebecois (9.98 per cent and 15.9 per cent), New Democrats (18.18 per cent and 12.0 per cent), and Greens (6.78 per cent and 0.0 per cent). Since the founding of the federation in 1867 there has been only one coalition government, the so-called Union government (1917-20). The coalition was aimed at broadening the support for the government of Robert Borden (Conservative) and its controversial conscription policy during the World War I. The Conservatives prizing the British connection announced conscription, while the Liberals led by the French Canadian Wilfrid Laurier disagreed. The policy was opposed by many Canadians, especially the French Canadians in Quebec and rural farmers generally. Many English-speaking rebel Liberals broke ranks and joined the Union government which also won the general election of 1917 and pushed the conscription policy through Parliament. At the provincial level coalition governments have occurred in Western Canada: in Manitoba the Liberal-Progressive combine in 1931 and the non-partisan all-party government in 1940 to meet the wartime demands, and in British Columbia the Liberal-Conservative wartime coalition to keep the Cooperative Commonwealth Federation (CCF) at bay. Having become wary of the divisive coalition governments, Canadians now prefer to form minority governments in hung Parliaments. The examples are the Liberal government of Pierre Elliott Trudeau in the early 1970s, the Conservative government of Joe Clark (1979-80), and the minority government following the three back-to-back electoral victories of Liberals led by Jean Chretien until 2000. Minority governments in Canada have not always been unstable.
The historic model of a “stable two-and-a-half party system” in Canada has been shattered in which the two “Parties of Consensus” (Liberals and Conservatives) accounted for over three quarters of vote and the remainder (under 20 per cent) going to a “third party” (The Cooperative Commonwealth Federation earlier, but lately New Democrats). The veteran analyst of the party system in Canada Hugh Thorburn (2001:8) expresses the puzzle “Whither Canada?”

In Australia since the founding of the federation in 1901, two national parties have dominated politics: the Labour Party representing the organized working class and a coalition of non-Labour political interests into two other parties that may be viewed for all practical purposes as a single party. The latter is “a centre-right party that has been predominantly socially conservative and with a base in business and middle class, now the Liberal Party of Australia; and a rural or agrarian conservative party, now the National Party of Australia”. These three parties or social forces have been systemically relevant since the beginning of the 20th century at federal as well as provincial levels “and only on rare (and generally short-lived) occasions have any other parties or independents played a role in formation or maintenance of governments”. (http://en.wikipedia.org/wiki/Politics_of_Australia:2, accessed on 19.9.2009). Liberals and Nationals have been in a long-standing coalition federally but not always at the state level nor has the Liberal Party always been the senior partner, e.g. Queensland is dominated by the National Party. The coalition between these two parties has been consistent though electorally in at least some constituencies the electorate may have an effective choice among three parties. Intra-party discipline in Australia is extremely high as in other White Commonwealth Parliaments.

New Zealand for well over half a century was governed by single-party majority governments. Earlier, from 1931 to 1935 there was a coalition government between the two of the three major parties of those days, the Liberal Party and the Reform Party to tackle the Great Economic Depression that began in 1929. In the aftermath of the depression these two conservative parties merged to obviate the victory of the Labour Party due to split in the anti-Labour vote and carried the day with 55.4 per cent of the vote. Between 1935 and 1993 the winning party won an average of 58.1 per cent of parliamentary seats with an average of 46.6 per cent of the total vote. This vote-seat discrepancy averaged 12.0 per cent of votes but only 0.1 per cent of seats. In 1993 the
Labour Party and the National Party together registered 69.8 per cent of votes but 96.0 per cent of the seats (McRobie 1997: 331-32).

After the switch-over to proportional representation, the first parliamentary election in New Zealand under the new electoral law was held in 1996. Commenting on this historic election, Roberts (1997:131) wrote: “Six parties are represented in the new Parliament, each in close accord with share of the votes it won throughout the country as a whole: the system is highly proportional [in terms of parties and ethnic groups]”. In the latest elections held in 2008 five parties counting only those winning more than one seats are represented in the Parliament: National (electorate vote share 46.6 per cent / seat share 47.5 per cent), Labour (35.2 per cent / 35.2 per cent), Green (5.6 per cent / 7.38 per cent), ACT (3.0 per cent / 4.11 per cent), and Maori (3.3 per cent / 4.11 per cent) (Jack Vowles, 2009).

South Africa is a rather recent entrant to multi-party democracy with more than a dozen parties in the National Assembly. In the wake of the first multi-party elections in 1994 the African National Congress (ANC) emerged as the predominant party with an overwhelming majority of seats in national and provincial legislatures in a tripartite combination of the ANC, South African Communist Party (SACP), and the Congress of South African Trade Unions (COSATU). In a conference of political forces called Convention for Democratic South Africa (CODESA) a deal was agreed upon to proceed for a constitutional provision in favour of a Government of National Unity (GNU) for the first five years to pave the way for wider political participation in reconciliation and transformation of the nation. A coalition cabinet comprising the ANC, the National Party (NP), and the Inkatha Freedom Party (IFP) was formed after the 1994 election. It was called a compulsory constitutionally mandated coalition government politics. In 1996 the NP decided to withdraw from the GNU coalition government. The second general election in 1999 led to another coalition government called Democratic Alliance (DA) led by ANC and comprising Democratic Party, New National Party (NNP), Federal Alliance (FA) electorally eying specific provinces (Western Cape, Guateng, and Kwa Zulu Natal), where demographic and political factors appeared to be on their side. But the DA put up candidates for only 200 local government seats, leaving the rest open for other parties. No party was able to win an outright majority in Kwa Zulu Natal and Western Cape, and ANC and IFP formed a coalition government in the former province. The NNP, DP, and FA formed a coalition government in Western Cape, keeping the ANC out (Olaleye 2003:2-3).
The ANC has maintained its decisive dominance in national politics in the 2004 and 2009 general elections with 69.68 per cent of registered voters in the former and 65.90 per cent in the latter. This one-party dominance has continued in a multi-party framework, with DA retaining the second party position bagging 12.37 per cent of popular vote in 2004 and 16.66 per cent in 2009. With the mandatory coalition government under the 1994 constitutional agreement having been dispensed with in the 1996 constitution, ANC has proceeded to rule with its majority party governments. It had also largely benefited from a set of the 2002 constitutional amendments allowing elected representatives at all levels of governments floor-crossing to another party and formation of new political parties. In the 2009 general election four political parties won double-digit seats in the National Assembly: ANC 264, DA Party 67, Congress of the People (COPE, a new party) 30, and IFP 18 (South African general election, 2009-Wikipedia: 1-4; accessed on 26 September 2009).

South Africa faces formidable challenges in its second decade of democracy. The greatest political problem before the pre-democratic regime was to deal with blatant discriminations against the Black majority. The most serious task before the democratic regime is to tackle the growing alienation among the minorities, White and non-Black-and White as well as sections in the Black majority. The peaceful transition to democracy and federalism and its maintenance since 1994 is a great achievement. Also on the asset side is a more active civil society historically and politically. Nevertheless, there are uncertainties as well. “The overwhelming political power of South Africa’s dominant party and the risks it poses to both the competitiveness of the multi-party system and authority of the constitution should not be underestimated” (Brooks 2004: 21). The ANC since democratization has been led by a Black beginning with Nelson R. Mandela and the main opposition party DA by a White, the present leader being Helen Zille (2009). The democratic future of South Africa lies in a combination of consociational and federal and coalitional governance.

While the problem of South Africa is democratic consolidation, India may be cautiously said to have crossed this threshold. Its one-party dominant system under the aegis of the Indian National Congress transited to a multiparty system of polarized pluralism in 1989. The number of systemically relevant parties at the national level has increased from over half a dozen in 1989 to one-and-a-half to double this number in the decades that followed besides several regional parties dominating or effectively competing in state
Working of Coalition Governments in Comparative Perspective

politics and playing decisive balancing role in federal coalition governments. This exercise in federal coalition or minority governments began in 1989 though there was also a brief interlude of *de facto* coalition government in New Delhi under the Janata Party, a political formation produced by hurried merger of five non-Congress and non-Communist parties on the eve of the 1977 Lok Sabha election following the end of the quasi-democratic emergency regime of Indira Gandhi (1975-77) (Singh 2005; Roy 2005). Federal coalitions got off to a bumptious start with frequent fall of governments and recourse to fresh mandates from 1989 to 1991 and then again from 1996 to 1999: two governments in the first unstable spell and three in the second. A minority Congress government led by the veteran P.V. Narasimha Rao governed a full term (1991-96) and so did a BJP-led National Democratic Alliance government headed by Atal Bihari Vajpayee (1999-2004) and a Congress-led United Progressive Alliance government stewarded by Prime Minister Manmohan Singh and Congress President and UPA National Advisory Council chairman Sonia Gandhi (2004-09). The latter was re-elected in 2009 with the increased strength of the leading party in the UPA and the Parliament.

The cynical view of federal coalition governments maintains that they are non-ideological and largely motivated by political and personal opportunism. This perception is reinforced by the fact that in some vital areas of public policies one looks in vain for different ideological or programmatic thrusts in different sets of coalition governments that have come and gone. Since the neoliberal shift in the economic policy regime in 1991, for example, at least three sets of coalition governments may be delineated: (a) Janata Dal-led National Front and United Front governments, (b) Congress minority or Congress-led UPA governments, and (c) BJP-led NDA governments. Going by professed ideology or programme, Janata coalitions have been left-of-centre progressive ruralist, congress-led coalitions have been left-of-centre progressive, and BJP coalitions have been right-of-centre Hindu neo-traditionalist or centrist-secularist. Once neo-liberal capitalist reforms were embraced under compulsions of an economic crisis in 1991, the direction of economic policies under various coalitional dispensations have hardly changed, notwithstanding some readjustments in the pace of reforms. Indeed, even diametrically opposed left front state governments in West Bengal and Kerala sooner or later fell in line, reorienting their economic policies in the states under their rule while opposing similar policies in the Parliament! The differences among the various coalition governments in New Delhi have been more sharply reflected in the domain of cultural and regional policies in deference to the ethnic and regional composition of the electoral bases of the
leading and supporting parties in the government concerned. Differences among various coalition governments in New Delhi on foreign and defence policy issues have also been blurred. For example, it was the BJP-led NDA government that started the strategic dialogue with the US government and the Congress-led UPA-I government finalized the Indo-US civilian nuclear deal in 2009 making the signatories strategic partners if not allies. Only the communist parties were consistently opposed to this deal; and when the leftwing supporting the Manmohan Singh government from the floor in the Parliament (without jointing the cabinet) deserted on this issue, the Samajwadi Party bailed the government out (Singh 2001, 2004; Chakrabarty 2005; Adeny and Saez 2005).

Coalition governments in Indian states started much earlier than at the Union level. The Congress-Praja Socialist Party coalition government led by Pattom Thanu Pillai in Kerala dates back to the 1950s. In the wake of the fourth general elections in 1967, the then dominant Indian National Congress ruling in New Delhi as well as in practically all states lost in eight of the then 16 states, even though it was voted back to power with reduced majority at the national level. Practically all major states of north India were lost by the Congress. In all these states in the north a hotchpotch set of non-Congress coalition governments came to be formed. Since the only bond in these formations was their antipathy to the Congress Party, and as they included parties from the right to the left, they turned out to be houses of cards that collapsed under their own internal ideological or programmatic contradictions (Brass 1968). They were soon elbowed out of their tenancy in state-level power by a rehabilitated Congress Party under Indira Gandhi by 1971-72 and thereabout.

However, by the late 1970s some stable coalition governments of the left front surfaced in West Bengal and Kerala and after a while in Tripura. The Left Front in West Bengal with a distinct social democratic policy thrust has continuously been in power since 1977 and has developed well-settled norms and procedures of coalition governments, which has elicited appreciative studies by Indian as well as foreign observers. The CP(M)-led Left Democratic Front and Congress-led United Democratic Front governments have also set a standard of stable and policy-oriented governments. Tripura is also a chip of the same block (Nossiter 1982, 1986; Desai 2007).
The key to the stability of coalition governments lies in the structure of the party system in India and for that matter in any representative and responsible government. Reflecting on the party political processes and governance in parliamentary federal India, Douglas V. Verney (2008: 1) remarks:

“If the trend away from the two largest parties, classified as ‘National Parties’ continues, government will become even more dependent on small so-called ‘State Parties’ nearly all of which are confined to a particular region. India’s politics could come to resemble the unstable regime of the French Third Republic.”

The remedy proposed by Verney (2008) is to offer incentives and encouragement to new National parties based on interstate alliances of smaller parties. These new parties could then be classified as National Interstate parties and would parallel the two present nation-wide parties - the Indian National Congress and the Bharatiya Janata Party - , which in turn may be classified as National All-India parties. This would reduce the dependence of federal coalition governments on small regional parties holding the governments to ransom and destabilizing them for petty political opportunism. (Verney 2008: 30). is, however, sure that the reform proposed by him “is not likely to occur unless there is a crisis.” This crisis obviously means a crisis of acute intractability in formation and maintenance of government.

Part III

West European Parliamentary, Parliamentary-Federal, and Presidential-Federal Systems

This class of political systems in this study consists of the Belgium, Netherlands, Luxembourg, Austria, Germany, Sweden, Norway, Italy, Spain, and Switzerland. These West European political systems here discussed in relation to coalition government are all fairly developed both in economic and political terms. Only Spain was politically less developed until the 1970s when it joined the ranks of democratic countries belatedly as part of Samuel R. Huntington’s (1991)”third wave” of democracy. In terms of seven patterns of modernization postulated by comparative historian C.E. Black (1966/1967: Chapters 3 and 4) all these countries belong to the third pattern after the first pattern charted by the pioneers (United Kingdom and France) and the second pattern joined by
the United States by the United States and the White Commonwealth, i.e. Canada, Australia, and New Zealand. The consolidation of the modernizing leadership took place earliest in Belgium and the Netherlands and Luxembourg during 1795 and 1848 (1867 in case of Luxembourg). Switzerland followed closely on their heels during 1798-1848. Germany followed suit early with the turn of the century in 1803-1871. Italy was not far behind (1805-1871). Spain came a little later in 1812-1909. Austria was the last in this group to experience the consolidation of modernizing leadership during 1848-1918. Similarly, in accomplishing the task of economic and social transformation Belgium, the Netherlands, and Luxembourg were again in the lead in this group of countries. The first two turned this corner between 1795-1848 and Luxembourg between 1867-1948. The corresponding periods for Switzerland were 1798-1848, for Germany 1803-1871, for Spain 1812-1909, and for Austria 1848-1918. This process began in Italy in 1871 and inconclusively lingered. Likewise, integration of society was begun by Belgium, the Netherlands and Luxembourg by 1948, by Switzerland by 1932, and by Germany by 1933, whereas Italy, Spain and Austria had not crossed this threshold even until the mid-1960s when Black published his book.

Table-4 presents an overview of the cultural cleavages in the West and South European polities under review on the basis of their demographic profiles for the present. Overall, cultural diversities in these countries are patent, but not extreme.

<table>
<thead>
<tr>
<th>Countries</th>
<th>No. of Religious Groups (1% +)</th>
<th>No. of Linguistic Groups (1% +)</th>
<th>No. of Ethnic Groups (1% +)</th>
</tr>
</thead>
<tbody>
<tr>
<td>The Netherlands</td>
<td>2 (Christian, 51%; Muslim, 5.5%)</td>
<td>3 (official language Dutch and several regional languages and dialects)</td>
<td>6 (80% Ethnic Dutch, 2.29% Turkish)</td>
</tr>
<tr>
<td>(Population 16,499,084 in 2009)</td>
<td></td>
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<td></td>
</tr>
<tr>
<td>Country</td>
<td>Population</td>
<td>Religion</td>
<td></td>
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<td>------------------</td>
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</tr>
<tr>
<td>Austria (Population 8,210,281 in 2009)</td>
<td>2 (78.3% Christian, 4.2% Muslim)</td>
<td>1 (94% German, 6% Bavarian, 6% Alemanic. German is the official nationwide language)</td>
<td>3 (91.1% former Yugoslavs, 1.6% Turks, 0.9% Germans)</td>
</tr>
<tr>
<td>Germany (Population 82,220,000)</td>
<td>2 (62.2% Christian, 4% Muslim, 2% Orthodox)</td>
<td>8 (95% German, the only official language, and 7 protected minority regional languages)</td>
<td>No data on ethnic groups provided</td>
</tr>
<tr>
<td>Italy (Population 58,126,212)</td>
<td>2 (90% Christian, 7% irreligion, 2% Islam)</td>
<td>Italian is common and official language with several officially recognized minority languages in regions</td>
<td>4 (94% Italian, 3% other Europeans, 1.3% North Africans, 1.7% others)</td>
</tr>
<tr>
<td>Spain (Population 46,157,822)</td>
<td>2 (80.4% Roman Catholic, 2.3% Other)</td>
<td>5 (89% Spanish, mother tongue, 9% Catalan MT, 5% Galician MT, 1% Basque, 2% Aranese)</td>
<td>No data on ethnic groups provided</td>
</tr>
<tr>
<td>Belgium (Population 10,414,336 in 2009)</td>
<td>2 (75% Roman Catholic, 3.5% Muslim, small minorities of Protestant Orthodox, Anglican and Jew)</td>
<td>3 (60% Dutch, 39% French, less than 1% German. All three official languages)</td>
<td>No data on ethnicity provided</td>
</tr>
<tr>
<td>Denmark (Population 5,447,084 in 2007)</td>
<td>Above 83% Lutheran Christian and several other Christian groups and religions are officially recognized as minorities</td>
<td>Danish is the dominant official language and four minority languages are regionally official or co-official</td>
<td>Danes are the dominant ethnic group with half a dozen minority ethnic groups largely based on tribes and nationalities.</td>
</tr>
<tr>
<td>Country</td>
<td>Religious Composition</td>
<td>Language and Minorities</td>
<td>Ethnicity</td>
</tr>
<tr>
<td>--------------</td>
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</tr>
<tr>
<td>Sweden</td>
<td>Above 78% Lutheran Christians + others Christian denominations and other religious minorities</td>
<td>Swedish is the dominant and official language and five officially recognized minority languages in some municipalities</td>
<td>Besides the Sweden, the Sweden Finns are the largest ethnic minority among others.</td>
</tr>
<tr>
<td>Norway</td>
<td>90.5% Christians (86% Lutheran) 2% Islam, among others</td>
<td>Norwegian is the dominant and official language and five other languages are official languages in some municipalities</td>
<td>Ethnically predominantly Norwegian among some other ethnic groups</td>
</tr>
<tr>
<td>Switzerland</td>
<td>2(79.9% Christian, 4.3% Muslim)</td>
<td>4 (63.7% German, 20.4% French, 6.5% Italian, 0.5% Romansh. All four official languages</td>
<td>No data on ethnic city provided</td>
</tr>
</tbody>
</table>

**SOURCE:** Gleaned from Wikipedia in September 2009.

**NOTE:** Percentages in several columns do not add up to 100 as categories ‘Other’ and ‘None’, etc. are omitted. Some of these categories in some countries may be quite sizeable, e.g. persons “without any region” in Switzerland are as much as 11.1 per cent.

All are Christian-majority countries, ranging from 90.5 percentage point in Norway to 51 per cent in the Netherlands. The second religious minority in none of these countries exceeds more than 5.5 per cent. Muslims are largest single minority in Norway and practically all of these nations ranging from 5.5 per cent in the Netherlands to 2 per cent in Germany (We do not have exact data on this dimensions beyond the information that Luxembourg is predominantly Roman Catholic in population.). Lutheran Christian church is state-supported in Denmark and Norway and was so in Sweden until 2000 when it was formally separated from the state. Religious freedoms are constitutionally guaranteed to all religions, including those whose numbers are small, in all the three Scandinavian countries.
Linguistic diversity is of greater moment in these countries than the religious. Danish, Swedish, and Norwegian are the dominant and official languages in Denmark, Sweden, and Norway. Though German is the dominant linguistic group in Germany (95 per cent) and Austria (94 per cent), and in the majority in Switzerland (63.7 per cent), there are significant linguistic minorities in all these countries. German is the only official language in Germany and Austria, but there are seven protected minority regional languages in the former and six Alemanic minority languages in the latter. The dominant linguistic group in Spain is Spanish (89 per cent) and the majority linguistic community in the Netherlands is Dutch. These are also the sole or the major official languages in these two countries. There are three official languages each in Belgium (Dutch, French, and German) and four in Switzerland (German, French, Italian, and Romansh). Luxembourgish is the national and official language in Luxembourg, but French and German are also administrative languages. Dominant ethnic groups in the three Scandinavian countries are the Denis, Swedes, and Norwegians, among others in each, though their numbers are not sizeable.

The dominant ethnic groups in Austria are former Yugoslav (91.1 per cent) and in the Netherlands, the ethnic Dutch (80 per cent). The four other countries do not provide data of “ethnicity”. The 1978 Spanish constitution define the “Spanish people” as the nationality of the country, though the preamble to the Constitution also speaks of the “peoples of Spain” and their respective cultures, traditions, languages, and institutions. The country is still struggling to integrate the official Spanish nation in the midst of strong ethnic regional identities, some also fostering separatist movements.

The existence of moderate to major cultural cleavages in our set of European countries and the prevalent use of proportional representation in all of these cases (see Table-5) creates a strong likelihood of multi-party system and coalition governments. This expectation is actually met. As a matter of fact, it seems to me that the party system fragmentation in these countries is more due to proportional representation than the social and cultural cleavage that is of moderate rather than extreme kind. Coalition or minority governments are a normal state of affairs in all these countries with parliamentary government (the Netherlands and Italy) or parliamentary-federal governments (Germany, Spain, Belgium, Austria). In presidential-federal Switzerland there has been a four-party power-sharing agreement called “magic formula”. This has been put under some strain as the rightist Swiss People’s Party (SVP), traditionally the junior partner, more than doubled its vote share from 11.0 per cent in 1987 to 22.5 per cent in 1999. The typical pattern of
seat sharing in the seven-member cabinet had been 2 for Free Democrats, 2 for Christian Democrats, 2 for Social Democrats, and 1 for Swiss People’s Party. The last mentioned took one additional position from Christian Democrats in 2004.

Table 5

Forms of Government and Systems of Representation in West European Political Systems

<table>
<thead>
<tr>
<th>System of Representation</th>
<th>Form of Government</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Parliamentary</td>
</tr>
<tr>
<td>Proportional</td>
<td>The Netherlands (List PR)</td>
</tr>
<tr>
<td></td>
<td>Luxembourg</td>
</tr>
<tr>
<td></td>
<td>Italy (List PR pre-1993 referendum, thereafter Additional Member System largely predicated by a majoritarian electoral system)</td>
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<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
</tr>
<tr>
<td>Plurality or FPTP</td>
<td>X</td>
</tr>
</tbody>
</table>

Europe is largely a continent of multiparty systems. Colomer (2008:9) remarks that “restrictive, close to two-party systems favouring single-party governments exist [only] in Greece, Hungary, Ireland, Malta, Spain, and the United Kingdom.”

Table 6 offers a synoptic overview of the party systems and coalitional governance in the polities under review here. In all the six European polities here the invariant pattern found is of multi-party systems with coalition governments. We will discuss each of these instances in brief elaboration in turn, and then finally offer some overall generalizations. In the Netherlands no single party has ever been able to get a majority in Parliament since 1900, necessitating two or often three parties joining hands to form a coalition government.
The head of the state in this parliamentary monarchy sets the ball rolling with secret individual meetings with the presiding officers of the Senate and the House of Representatives. This is followed by meetings with the leader of each parliamentary party in the House of Representatives.

### Table 6

**The Party Systems in West European Polities**

<table>
<thead>
<tr>
<th>Country</th>
<th>Party System Characteristics</th>
</tr>
</thead>
<tbody>
<tr>
<td>Denmark</td>
<td>A multi-party system comprising 19 parties, with no single party getting absolute majority in the Parliament since the beginning of the 20th century. Mostly minority coalition governments formed.</td>
</tr>
<tr>
<td>Sweden</td>
<td>A multiparty system consisting of 18 parties but the Social Democratic party has historically played the leading role; only the general elections of 1976, 1979, 1991, and 2006 have given the centre-right bloc enough votes to form coalition governments.</td>
</tr>
<tr>
<td>The Netherlands</td>
<td>A multi-party system with 10 parties (in 2007) with inevitability of coalition governments.</td>
</tr>
<tr>
<td>Germany</td>
<td>A multi-party system with 7-odd parties (in 2005). Coalition governments are the norm.</td>
</tr>
<tr>
<td>Austria</td>
<td>A multi-party system with five major parties. Since 1980s four major parties have consistently registered enough votes to win seats in the national Parliament.</td>
</tr>
</tbody>
</table>
The constitutional monarch then designates an *informateur* who explores the possibility of a new cabinet. Typically the *informateur* is a retired veteran politician with a background in the largest party in the House of Representatives. The Queen often directs the *informateur* to seek a coalition of parties with programmatic compatibility and a majority in the House. If the first *informateur* is bogged down then a second is floated.

<table>
<thead>
<tr>
<th>Country</th>
<th>Political System</th>
</tr>
</thead>
<tbody>
<tr>
<td>Switzerland</td>
<td>A multi-party systems since 1959 four major parties have formed the “magic formula” (“Zauberformel”) according to which they share the seven cabinet positions.</td>
</tr>
<tr>
<td>Italy</td>
<td>A one-party dominant system under the aegis of the Christian Democratic Party until the end of the 1980s and a multi-party system since the early 1990s.</td>
</tr>
<tr>
<td>Spain</td>
<td>A <em>de facto</em> multi-party system. At the national level a party system similar to a two-party system in which the two dominant parties control electoral routes to the Parliament, but regional parties are strong in autonomous communities like Catalonia and the Basque Country whose support is essential for coalition governments.</td>
</tr>
<tr>
<td>Belgium</td>
<td>One of the most fragmented party systems in modern democracies. A multi-party system with a pillarized cartel of party elites that counterveils the centrifugal trends. The main Belgian political parties, although split into Flemish and Walloon organizations mainly competing at the regional level but still maintaining a national government where regional coalitions are also forged. The federal dimension still survives as central institutions reinforce themselves and Belgium somehow operates as a single entity in the European Union domain (Pugaciauskas 2000)*.</td>
</tr>
<tr>
<td>Luxembourg</td>
<td>Multi-party system</td>
</tr>
</tbody>
</table>

All the Scandinavian parliamentary systems with constitutional monarchies in Denmark, Sweden, and Norway have multiparty systems with an unusually large number of parties attributable more to proportional representation and populist-social democratic tradition than to cultural diversities. Denmark and Norway have been mostly ruled by minority and/or coalition governments, whereas Sweden has mostly been under majority Social Democratic Party governments, expecting the general elections of 1976, 1979, 1991, and 2006 which yielded centre-right coalitional dispensations. The Swedish Social Democrats have been the leading political force since 1971 when the Refomists wrested control of the party and the Revolutionaries were driven out. This is supposed to be the reason of the post-war Swedish welfare state with government expenditure accounting for slightly more than 50 per cent of the gross domestic product (GDP).

The Lipset- Rockken (1967) thesis on the “freezing of social cleavages” hypothesis offered to explain the stability of western European party systems has been rejected elsewhere in the region (Mair 2009), but it is still supposed to hold in Scandinavia (Sundberg 2002/2009; Berglund and Lindstrom 2006/2009). S.M. Lipset and Stein Rokkan had written in 1967: “The party systems of the 1960s reflect, with few but significant exceptions, the cleavages structures of the 1920s …[T]he party alternatives, and in remarkably many cases the party organizations, are older than the majorities of the national electorates” (quoted in Mair November 2003: 1). Sunburg (2002/2009: Abstract) argues that the Scandinavian party systems in large parts are still frozen as the diminishing class voting and electoral instability are unreliable measures of how well cleavages structures are reflected in the party systems as the struggle between three pole party fronts to incorporate new categories of voters is the very essence of an enduring cleavages structure in these countries. Similarly, Berglund and Lindstrom (2006, 2009: Abstract) in a study of party systems in Finland, Sweden, Denmark, and Norway conclude: “The social changes which manifested themselves in the early ‘70s, most notably the decrease in class voting, were not dramatic enough to undermine the class character of the party systems. Even the new arrivals make sense in a left-right perspective. The drop in class voting was an asset to whatever party knew how to make advantage of it; and the realigning elections in the early part of this decade testify to the unwillingness rather than the inability of most parties to do so.”

In the 2006 Netherlands elections as many as 11 parties maintained parliamentary presence, but the major parties are Christian Democratic Appeal (CDA), Labour Party
(PvdA), Socialist Party (SP), and People’s Party for Freedom and Democracy (VVD). These four parties together accounted for 80.67 per cent of the House of Representatives seats and 81.33 seats in the Senate in 2006. This election saw some significant changes in the relative party positions. The Socialist Party almost tripled its parliamentary strength, while the moderate Labour Party lost a quarter of its seats. At the other end of the political spectrum LPF lost all its seats and a new anti-immigrant party PVV went from zero to six per cent. The negotiations, made difficult by the increased left-right polarization, finally led to the formation of the fourth Social-Christian government by the PvdA, the CDA, and the Christian Union.

The multi-party system with coalition governments has been a long-term feature of Luxembourg politics. Since 1962 there have been some internal changes in the complexity of the party political scene with formation of new parties, and since 1974 the Communist Party suffered steady decline and after 1994 disbanded itself and reformed into the New Left Party. Since 1919 the Chrishan Social Party (CSV) had led every governing coalition, but in 1974 it lost in an election dominated by abortion rights, women’s rights, and inflation among other issues. It remained the largest party, but reigns of power passed on to a coalition of Socialist Workers’ Party (LSAP) and the Democratic Party (PD) also called the Liberals. However, in the 1979 election the CSV regained its dominance in alliance with PD and remained in the saddle until 1983/84. In 1984, after agreeing to wage indexation without reduction of the 40-hour work week, CSV formed a coalition government with the LSAP and ruled for the next 15 years. Despite the formation of new parties like Action Committee for Democracy (also known as Pensioners’ Party in a country with growing population of the old), Green Alternative Party (GAP/Dei Greng), Green List Ecological Initiative (GLEI), and the New Left, the CSV and LSAP remained partners in the ruling coalition until the 1999 election. “At this point, the inclusion of a party other than the CSV, LSAP, and PD in a governing coalition seems a long way off” (Graubart 200:1). In the 2000 election these three parties together accounted for 75.6 per cent of votes and 80 per cent of parliamentary seats.

Historically, the Dutch party system in the first half of the twentieth century presented an image of “a pillarized society where two cleavages, one religious and the other socio-economic, acted to determine social and political loyalties”. Since the 1960s the party system changes have gradually unfrozen the foregoing pattern of the “freezing
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hypothesis” of the Lipset-Rokkan characterization of the European party system as applied to the Netherlands and weakened the pillarized structure of the polity (A. Tan, n.d.:221)

In the first post-World War II election based on universal adult franchise in Italy held in 1948, the Christian Democratic Party won against the United Front of the Communist and Socialist parties and remained the dominant political force for four decades. Yet this dominance was composite one as illustrated by the inclusion of the Socialist Party in the government in the 1960s. Christian Democrats tried to include the Communist Party as well in the government, but this so-called “historic compromise” failed. During the 1980s the Communist Party gradually increased its vote, and in the 1984 election the Christian Democrats for the first time failed to emerge as the largest single party. By the beginning of the 1990s in the midst of extensive corruption in public life the Christian Democratic Party and the Socialist Party disbanded, and the communists under a new name, Democratic Party of the Left, became the main social democratic party of Italy. Under a new majoritarian electoral law introduced after the 1993 referendum, the 1994 election witnessed rise of new political parties and a massive electoral realignment. Italy was ruled by a series of centre-right coalitions between 1996 and 2001. By the late 2000s a centre-right coalition took reigns of power. The centre-right coalition comprising three parties won again in the 2008 election.

Competent observers remark that the French political system fuels anxiety “by the fact that the rules of the game, the procedures, the institutions are not fully established. They are not stable because both the debate concerning which institutions and the attempt to reform them seem to be heading in a partisan rather than systematic direction. Unless, and until such time as, a single player or coalition of players succeeds in formulating new rules and constructing new institutions, the Italian political system and its democracy will continue to be object of pervasive criticism, and understandably so. In sum, the proof of the vitality of Italian democracy is that it is still, changing. The level of citizens’ dissatisfaction with its functioning but not with its principles, is evidence that enough Italians care about improving it”(Pasquino 2008: 171-2).

Germany has a multi-party system with two large parties – Christian Democratic Union (CDU)/Christian Social Union (CSU) and Social Democratic Party – and three substantial smaller parties – free Democratic Party (FDP), the Left Party (formerly the
Party of Democratic Socialism), and Alliance ‘90/The Greens. The Christian Democrats (“sister parties” that avoid direct electoral contests in the same regions) are right-of-
centre or conservative, Social Democrats are left of centre, Free Democrats are liberal
(currently neoliberal), the Left Party is socialist, and the Alliance ‘90 are green. In addition,
there are also some minor parties with marginal parliamentary representation. In Germany
coalition governments are the norm as it is rare for either the CDU/CSU or SPD to win a
majority of their own. Thus coalitions are formed with at least one of the substantial
smaller parties. Helmut Kohl’s CDU government ruled for years in coalition with FDP,
Gerhard Shroder’s SPD was in power with the Greens, and at this writing (September
2009) the centre-right coalition of CDU and its pro-business ally, the Free Democratic
Party, have just been re-elected. The alliance led by CDU, its Bavarian conservative sister-
party, the Christian Social Union, and the FDP won 48.4 per cent of the national vote
under the leadership of Chancellor Angela Merkel.

The dynamic stability of the German party system has not escaped the general
trend of the decline of membership, appropriation of some of the functions of political
parties by other organizations and agencies, “personalization” of the executive, etc. Yet
“the durability of the German political parties as collective actors and as dynamic
institutions have produced and maintained an evolutionary party system while still
producing the space or cushion necessary to prevent sclerosis or disintegration at an
institutional level” (Allen n.d.).

Austria is often considered an exception to the Duverger-Riker law that
proportional representation invariably leads to a multi-party system. Since 1949 party
politics in the country has been largely dominated by the conservative Austrian People’s
Party (OVP) and the Centre-left Social Democratic Party of Austria (SPO). Effective
competition and governance have been largely limited between two parties until the rise
of the third party, the Freedom Party in the 1980s and 1990s. The two largest parties
have had a Grand Coalition to keep the parties of the far left and far right out of
long hold on power, and rather than return to the Grand Coalition days of the 1960s
SPO decided to include a third, smaller party in the governing coalition. 1986 represented
a return to the Grand Coalition of OVP and SPO, which continued to be in command.
But a new element in politics is that the Green Alternative List Party broke through the
stranglehold of the three traditional parties, gaining four per cent of seats, a number that steadily rose over the ensuing decade. Yet 1990 saw the continuation of the SPO-OVP coalition, by and large. In 1995 the decline of the OVP continued. The FPO gains threatened the OVP on the right flank. On the other hand, the OVP electoral base was also eroded by the FPO splinter party, the Liberal Forum. However, the SPO continued to retain the FPO as the junior partner in the coalition government. In 1999 the SPO had its worst electoral performance in the post-war era, when it lost 25 per cent of its parliamentary seats. Negotiations for government formation between OVP and SPO failed. An OVP-FPO government was eventually formed, leaving the country’s largest party in the opposition for the first time in over forty years. When the FPO was first established in 1947 it was considered “a natural home” for ex-Nazis. The new government faced international stigma and outcries. In the subsequent elections the support for the Liberal Forum has steadily remained constant and the once minor parties now share roughly twenty per cent of popular vote. “This functioning multi-party environment”, writes Graubart (2000: 2) “is a far cry from the two and a half party system of the Austria of old”.

Since Spain’s transition to democracy nearly three decades ago following the four decades of authoritarian rule under General Francisco Franco party system has been in transition. Politics since 1993 has, however, been dominated by two major parties which have alternately been in power: the left-of-centre Socialist Workers’ Party (PSOE) and the conservative Partido Popular (PP). This dominance is a relative term as more often than not neither the PSOE nor the PP has enjoyed absolute majority in the Congress of Deputies. As a result, the largest party after an election has invariably formed a minority government sustained by agreements with one or more of the various minor parties. After the collapse of the middle-of-the road Socialist Democratic Centre (CDS, an offshoot of UCD) in 1993, the only nation-wide minor party in the parliament has been the United Left or Izquierda Unida (IU), a combination of the Spanish Communist Party and its cohort parties. Besides the foregoing three nation-wide parties at the national level, there is a significant number of regionalist or ‘nationalist’ parties that count as small parties nationally but have substantial electoral base in their respective regions. Catalonia has three ‘nationalist’ parties and the Basque Country has two such parties. Outside these two regions where linguistic nationalism runs high, Galicia and Canary Islands also have sizeable ‘nationalist’ parties (Alvarez-Rivera 2008).
The extremely fragmented nature of modern Belgian politics was polarized in alarming proportions in the aftermath of the June 2007 elections in this parliamentary federal monarchy. Following these excessively divisive elections, government formation took crisis-and-suspense-ridden nine months through the convention of putting together a governing coalition similar to that in the Netherlands described earlier. The five-party government took office under the clouds of uncertainty about its survival. “In most respects”, observes Castle (2008:1), “Belgium has two parallel political systems with different parties fielding candidates from the two biggest populations and appealing to voters through separate newspapers and television channels”. The new government comprises the Flemish and French-speaking Christian Democrats, the Flemish and French-speaking liberals, and the French-speaking socialists. The rabidly nationalist Flemish parties are in the opposition, but one of these is expected to support it. Yves Leterme, the leader of the Flemish Christian Democrats, almost heads a government of national unity which represents a broad spectrum of political opinion and more of big parties are parts of the coalition than outside (Castle 2008:1-2).

Table 7 presents some longitudinal aggregate data pertaining to membership in parliamentary cabinets in Western Europe between 1945 and 1999 (1 January). Counting the first World War II government until the beginning of the year 1999, it is found that coalition governments in Western Europe are far more frequent (69 per cent) than single-party governments (30.9 per cent). Indeed, in at least two countries – Luxembourg and the Netherlands – there have been no single-party governments at all. Such governments are also relatively less likely in Finland, Germany, Belgium, Austria, France, and Italy than in Sweden, Norway, Denmark, Ireland, and Portugal. Minority governments in Western Europe are relatively less frequent than single-party governments. Out of the 13 countries in the table, only four had minority governments with the incidence of 50 per cent or above. The mean number of political parties in party-based governments is relatively low. It ranges from 1.42 in Sweden to 3.49 in Finland. The West European mean for all the 13 cases is 2.3.
Part IV

Some Asian Parliamentary and Parliamentary-Federal Systems

We now examine the practice of coalition government in Japan, Israel, and Nepal. Unlike the previous groups of polities studied in the foregoing, this class of systems is most desperate as they are neither parts of a common institutional heritage (e.g. the British Commonwealth) nor of a common geographical and cultural area (e.g. the Western European Zone). They are also at different levels of economic development. While Japan is post-industrial, Nepal is post-traditional, whereas Israel’s position appears to be rather ambiguous on this dimension. In terms of C.E. Black’s (1966/1967 : Chapter 4) typology
of seven patterns of modernization, Japan in the mid-1960s was in the fifth pattern, having consolidated its modernizing leadership during 1868-1945 and begun socio-economic transformation in 1945 inconclusively then. Integration of its society was yet to be made. Israel and Nepal were both in the sixth pattern. The difference between the two was that the former witnessed the consolidation of its modernizing leadership during 1920-1948 and started its economic and social transformation in 1948, whereas Nepal had not reached these thresholds by the mid-1960s. None of these three polities had accomplished the integration of their societies by then. By now, all these three polities have traversed a tremendous distance and have seen radical transformations.

All the three polities in this category are in reality or popular perception relatively homogeneous in cultural terms. Pure or naturalized Japanese account for 98.6 per cent of the total population of Japan and 99 per cent of them speak Japanese as their first language. Israel is somewhat more diverse with 76 per cent Jews, 16 per cent Muslims, 2.5 per cent Arab Christians, among others. Hebrew and Arabic are the official languages of Israel. Though a large number of foreign languages are used, English being most common is also taught on a mandatory basis. Multilingualism and multicultural texture of the nation largely of immigrants is quite natural. Nepal’s population is 80.6 per cent Hindu, 10.7 per cent Buddhist, 4.2 per cent Muslim, among others. In terms of languages, 57 per cent of Nepalese are estimated to speak Nepali as their mother tongue; the percentages of other linguistic groups are as follows: Maithili 10 per cent, Bhojpuri 7 per cent, Tharu 4 per cent, and Limbu and Bajjika 1 per cent each. Hindi is widely understood, while many people in government and business are also conversant in English. Caste or ethnic groups number hundreds, but the two largest among these are Chhetris (15.80 per cent) and Bahun (12.74 per cent).

The form of government in all the three countries is presently parliamentary, though the Constituent Assembly of Nepal (elected in 2008) is at this writing (2009) engaged in drafting a parliamentary-federal constitution. The system of representation followed in Japan is the “parallel system” with ability to vote for both lists of positions grouped politically or according to organization, which, would then be elected proportionately and for individual names. Israel’s electoral law is based on the list proportional representation. The election to the Constituent Assembly of Nepal was directly held under a mixed system of representation, part of the seats filled in by plurality system and part of them by proportional representation.
Working of Coalition Governments in Comparative Perspective

The federal question in Nepal is fraught with the difficulty that “in most ethnically conceived federal units the dominant [major] ethnic/caste group will be in the minority relative to other ethnic caste groups that make up the total population of the unit”. Nevertheless, “the primary rationale for federalism in Nepal lies in breaking the shackles of a historically over-centralized state that has by design served the interests of upper-class Bahuns and Chhetris and has imposed their ethos on the rest of the country. Federalism in this sense should be an exercise in redefining and rediscovering Nepal” (Sharma 2008: 83).

The combination of cultural texture and form of government prevalent in the three case studies in this section would prompt a theoretical expectation for a two-party system in a common parliamentary set-up. This is inclusive of Nepal where before the Maoist rebellion and state of emergency that started in 2001 some variants of parliamentary or panchayat democracy was introduced with alternation and interruptions by the absolute monarchy since 1959. In 2008 Nepal became a republic and held Constituent Assembly elections under a mixed plurality and proportional system of representation. The new representational system in Nepal and the prevalence of variants of List PR in Japan and Israel set in motion a causation that favours a multi-party system.

As things really are, Japan and Nepal started with a one-party dominant systems, while Israel has had a multi-party system. The centre-right Liberal Democratic Party (LDP) continuously ruled in Japan from 1955 to 1993, when it was replaced by a minority government and multi-party system.

The immediate World War II years witnessed fragmentation of parties and a succession of minority governments in Japan. Under the US influence the governments also tried to suppress communism and followed anti-organized-labour policies. The conservative political forces, especially the Liberal Party and Democratic Party merged to produce the LDP as the dominant party within a multi-party framework which provided governmental stability until the early 1990s. In 1993 the LDP was voted out of power after 38 years of one-party dominance. A coalition of new parties and existing opposition parties formed a new government. The LDP regained political power in 1994 and ruled until 2009. A major turnaround came in Japanese politics in 2009 when the centre-left opposition Democratic Party of Japan (DPJ) won the elections and formed a coalition government with Social Democratic Party and People’s New Party.
Much more than the pattern of cultural cleavage, the electoral system of Israel, populist pretensions and emphasis on the power of Parliament (Knesset) make it very difficult to form and maintain governments in a highly fragmented party configuration. Coalition governments are an inevitable outcome, even these are unstable with average life a government being 22 months. The factors causing the fall of governments are commonly the issues relating to the peace process with Arab states, role of religion in the Israeli state, intrigues of smaller parties, and political scandals. Since the foundation of Israel in 1948, there has been only one single-party majority government between 1968-69. Coalition governments have been led by one of the three major parties. Since its inception Israel has been ruled until May 1977 by successive coalition governments (with one exception as mentioned above) led by the Labour Alignment (called Mapai before 1967). Out of this period a national unity government including all the parties was in saddle from 1967 to 1970. After 1977 the Zionist conservative Likud bloc of parties were in power, followed by a series of other coalition governments, e.g. the predominantly rightwing Benjamin Netanyahu government led by his Likud party (1996-1999), the Ehud Barak government based on an alliance of Labour, Meimad, and Gresher (1999-2001), the national unity coalition government led by Ariel Sharon of the Likud (2001-2006), the centrist Kadima-led Ehud Olmert government (2006-2009). The Kadima reemerged as the largest party in the Knesset in the 2009 elections (with 22.47% vote share/ 23.33% seat share), followed by Likud (21.61%/ 22.50%), Israel Beiteinu. (11.70% / 12.50%), Labour Party (9.93%/ 10.83%), Shas (8.49% / 9.17%). The remainder of 21.67 per cent of seats are distributed among 7 parties within the range of 5 and 3.

The turn of the century found the fledgling democracy in the Himalayan Kingdom of Nepal chartered on an uncertain course. Palace intrigues, ineffectual non-communist parties (the Nepali Congress Party being the largest among them), and the insurgent Maoist rebels created an extremely volatile political situation. A state of emergency, inconclusive attempts to end the deadlock by electoral process or military action, and an internationally brokered peace process by the Swiss government culminated in the election of a Constituent Assembly-cum-provisional Parliament in 2008. A coalition government led by the former Maoist rebel Kamal Dahal Prachanda, whose party won the largest number of seats, took office, with the Nepali Congress going into the opposition. The Communist Party of Nepal-Maoist-led coalition government included Communist Party of Nepal-United
Marxist-Leninist, and the ethnic-regional-based Mathesi People’s Right Forum. In May 2009 Prime Minister Prachanda resigned in protest against “unconstitutional and undemocratic” move by the President, Ram Baran Yadav, to block the sacking of the army Chief. Communist leader Madhav Kumar Nepal was named the new Prime Minister of the coalition government. The multi-party provisional Parliament is engaged in drafting a constitution of Nepal. The available pointers suggest that in all probability it would be a parliamentary-federal constitution similar in principle to that of India.

Part V

Presidential and Semi-Presidential Federations and parliamentary systems

In the preceding sections we have discussed coalition governments in parliamentary and parliamentary-federal systems in various parts of the world. This experience is of special relevance for India as it is itself a parliamentary-federal system. In this last substantive section prior to concluding my study, the coalition experience in a different institutional setting, i.e. presidential and semi-presidential systems and parliamentary systems would be examined. In the category of presidential systems, the USA, Brazil and Nigeria, have been selected here. In a way, the USA is a self-selecting case as it is the first presidential system in modern history as well as the only stable and institutionalized system of this kind in the world. Its institutional transplantation in any other country has invariably suffered instability and authoritarian degeneration. Another point to keep in mind is that the USA is not only presidential, it is also federal, and the first federal system in fact. Brazil in Latin America also happens to be a presidential-federal system, much in the US mould. So has been Nigeria since the revival of democracy there in 1999.

The USA, Brazil, and Nigeria considerably differ in terms of Black’s (1966/67: Chapter 4) seven patterns of modernization. The former belongs to the second pattern having consolidated its modernizing leadership between 1776 and 1865, crossed the threshold of economic and social transformation by 1865-1933. Brazil belongs to the fourth pattern, marked out by the consolidation of its modernizing leadership during 1850-1930, and begun the process of economic and social transformation by 1930. Nigeria is part of the seventh pattern where consolidation of modernizing leadership began
inconclusively so far in 1960, neither had it integrated its society when Black (1966/67) formulated his typology of modernization in comparative history and politics. Whether the task is accomplished today is also doubtful.

Examples of semi-presidential systems included in this study are France and Sri Lanka. Also known as presidential-parliamentary system, the term was first used by Maurice Duverger (1978) in a work in French to characterize the Fifth Republican constitution in France and subsequently elaborated it in English (Duverger 1980). It is based in a combination of presidential and parliamentary principles of government first attempted in France in 1958, following a long but incorrigibly unstable spell of parliamentary government. It juxtaposes a president directly elected by the people and a prime minister indirectly elected by the Parliament, which in the first instance is directly or popularly elected. To work the system it is thus necessary for the president and the prime minister to “cohabit” to govern. Sri Lanka, initially a parliamentary system after independence in 1948, switched over to a variant of semi-presidential system in 1978. These two cases selected here are prima facie very different in developmental terms. In terms of Black’s (1966/67: Chapter 4) seven patterns of political modernization, France belongs to the first, whereas Sri Lanka to the sixth. France underwent the consolidation of modernizing leadership during 1789-1848, experienced the economic and social transformation during 1848-1945, and began the process of integration of its society in 1945. The consolidation of the modernizing leadership took place in Sri Lanka during 1920-1948, the economic and social transformation began in 1948, while the integration of its society had not even begun when Black (1966-67) wrote, and by all available indicators is seriously problematic until now.

Let us now turn to the patterns of cultural cleavages in our cases of presidential and semi-presidential systems in review in this study. As Table-8 shows, the USA is culturally not all that diverse. It is predominantly Christian (76 per cent) with marginal non-Christian population segments (1.2 per cent Jewish and about 1 per cent Eastern religions). English is the sole official and spoken language from the Atlantic to the Pacific coasts and from the 49th Parallel (the US-Canada border) to the southern end. Some degree of ethnic diversity is there: 66 per cent non-Hispanic White, 15 per cent Hispanic White, 14 per cent African Blacks, and 5 per cent Asian Americans. The major source of diversity in the USA is geographical or regional.
### Table 8

**Cultural Cleavages in the Selected Presidential and Semi-Presidential Systems**

<table>
<thead>
<tr>
<th>Countries</th>
<th>No. of Religious Groups (1% +)</th>
<th>No. of Linguistic Groups (1% +)</th>
<th>No. of Ethnic Groups (1% +)</th>
</tr>
</thead>
<tbody>
<tr>
<td>USA (Population in 2009: 305,000,000)</td>
<td>2 (76% Christians, 1.2% Jewish, 0.9% Eastern Religions)</td>
<td>English, the sole official language</td>
<td>4 (66% Non-Hispanic Whites, 15% Hispanics, 14% African Americans, 5% Asian Americans)</td>
</tr>
<tr>
<td>Brazil (Population in 2008: 186,842,147)</td>
<td>1 (74% Roman Catholics, 15.4% Protestants, 1.3% Spiritism)</td>
<td>1 (Portuguese is the only official language + many Amerindian languages, native ones presently endangered</td>
<td>A single “Brazilian” ethnic group with varied racial types: 53% “White”, 38% “mixed”, 6% “Black”, 1% “other”</td>
</tr>
<tr>
<td>Nigeria (Population in 2005: 141,000000)</td>
<td>2 (50% Muslims, 40% Christians among traditional indigenous religions)</td>
<td>More than half of a dozen, including English (official), Hausa, Yourba, Igbo, Fulani, and others</td>
<td>More than 250 ethnic groups including Hausa and Fulani (29%), Yourba (20%), Igbo (20%), Calabar (10%), Ibibio (4.5%), Annang (3.5%), Efic (20%).</td>
</tr>
<tr>
<td>France (Population in 2009:65,073,482)</td>
<td>? (65% Roman Catholic, 12% some other religions, 27% consider themselves atheists)</td>
<td>1 (100% French with rapidly declining regional languages)</td>
<td>No official classification by ethnicity</td>
</tr>
</tbody>
</table>


Brazil down south in Latin America is again predominantly Christian (89.4 per cent), it is indeed the largest Roman Catholic country in the world. It is entirely Portuguese linguistically, with several non-official Amerindian languages that are presently endangered, especially the native ones. Ethnically, the country is supposed to be the home of a single “Brazilian” ethnic group, though with varied racial types: 53 per cent “white”, 38 per cent “mixed” and 6 per cent “Black”. Like in the USA, the major source diversity in Brazil is the vast geographical size of the country. Given the absence of major cultural divisions, the USA and Brazil could opt for a government of executive presidency with the singular political focus on the chief executive in the government as contrasted with the collegial cabinet government in a parliamentary system or collegial presidency in Switzerland. But regional diversity of these countries prompted them to go for a federal constitution.

Nigeria, the most populous country in Africa, is culturally very heterogeneous. Besides the Muslims and Christians, who account for about half and nearly 40 per cent of the population, there are other religious groups including “ethnoreligionists” and traditional religious faiths. More than half a dozen African languages are prevalent, but English is the sole official language of Nigeria. The ethnic diversity is even more complex with over 250 ethnic groups based on tribal origins.

France is a country without any major cultural contradictions, notwithstanding the recent violent religious protests perpetrated by immigrant workers of Muslim

<table>
<thead>
<tr>
<th>Country</th>
<th>Population</th>
<th>Religious Groups</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sri Lanka</td>
<td>19,238,575</td>
<td>4 (69.30% Buddhist, 15.48% Hindu, 7.56% Muslim, 7.62% Christian)</td>
</tr>
<tr>
<td></td>
<td></td>
<td>2 (Sinhala and Tamil are both official languages accounting for 74% and 18% of population respectively; English is commonly used in government and spoken well by 40% the population)</td>
</tr>
<tr>
<td></td>
<td></td>
<td>3 (73.8% Sinhalese, 3.9% Sri Lankan Tamil, 7.2% Sri Lankan Moors, 10% unspecified)</td>
</tr>
</tbody>
</table>

NOTES: The US religious data are form a survey, not census. The French religious data are form a study by the CSA Institute based on a 2003 sample survey.
background. The country is predominantly Roman Catholic (65 per cent, with 12 per cent of the population professing faith in some other religions. The country is 100 per cent French in linguistic terms, with rapidly declining regional languages. The French census does not use any ethnic classification in its decennial enumeration.

Historically, France was the first home of the European absolutist state as England was the first home of the moderate absolutism and gradual evolution of the parliamentary cabinet system. The absolutist state in France was destroyed by the Revolution in 1789, which was subsequently overtaken by the Bonapartist authoritarian state. Eventually, France went through a long spell of extremely unstable Assembly form of government subscribing to the principles of popular and parliamentary sovereignties. It was to contain these parliamentarist excesses that the De Gaulle constitution of 1958 was devised that designed what Maurice Duverger (1980) has conceptualized as the “semi-presidential system”, a new political system model.

In the group of countries being examined in this section, Sri Lanka is culturally the most diverse despite its considerably smaller size. Four major religious communities form the national community in the island republic in the Indian ocean adjacent to the Indian landmass across the Gulf of Mannar. These are: Buddhist 69.30 per cent, Hindu 15.48 per cent, Christian 7.62 per cent, and Muslim 7.56 per cent. Sinhala and Tamil are the two major linguistic communities accounting for 74 per cent and 18 per cent of population. Both are official languages, nationally and regionally, and English is commonly used as a functional medium by 40 per cent of the Sri Lankans. There are at least three major ethnic groups in the country: 73.8 per cent Sinhalese, 8.5 per cent Tamils, and 7.2 per cent Sri Lankan Moors. With this diversity and emerging from the British colonial tradition, Sri Lanka first began its career as an independent entity with a parliamentary form of government with considerable administrative thought favouring devolution and political pressure for federalism. In 1978 the country switched over to the semi-presidential system that indeed contributed to the excessive centralization of powers dominated by the executive presidency stamping out the tendency towards federalism and considerably whittling down devolution of powers to the “provincial” government that for all practical purposes are no more than weak local governments. This is the major political cause of the acute ethnic conflict and civil war since 1983 that ended in 2009 in the military repression of the Tamil militant separatists.

Table 9 presents a synoptic view of the forms of governments and systems of
representation in the group of countries under review here. The USA, the first presidential-federal system in the world, uses the type of electoral system that may be broadly called plurality/majority: it elects its national legislature by the plurality or the first-past-the-post voting system and elects the Presidents by a variant of plurality-majority system. This system of representation reduces the political diversity in the resulting elected institutions in a society that is not very diverse in cultural terms, which the US more or less happens to be. However, the regional diversity expressed in federalism is a factor that contributes to political pluralism and regional political diversity.

Culturally Brazil is moderately pluralistic, but regional diversity is considerable in this geographically large country. This diversity is further encouraged by a federal constitution and use of list proportional representation in electing the Chamber of Deputies, though the members of the Senate are elected by the majority electoral system. The President is elected by majority vote with run-off election (second round if the first round fails to yield majority).

The cultural diversity of Nigeria is easily manifested politically in the 36-state federal union (plus a federal capital territory) and 50 political parties at some points in time, despite the use of plurality-majority electoral system with open rather than secret balloting for parliamentary as well as presidential elections. Linguistic diversity of Nigeria papered over by the use of English as the role official language of the government(s). Recurrent ethnic violence and clashes over economic issues including gas pipelines and oil facilities are regular features of Nigerian politics. So were military coups prior to the 1999 revival of democracy.

<table>
<thead>
<tr>
<th>System of Representation</th>
<th>Form of Government</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Presidential-Federal</td>
</tr>
<tr>
<td>Plurality/Majority</td>
<td>USA (Since 1787)</td>
</tr>
<tr>
<td></td>
<td>Nigeria</td>
</tr>
<tr>
<td>Proportional</td>
<td>Brazil (Since 1988)</td>
</tr>
</tbody>
</table>
The French culture is fairly homogeneous. This trait is reinforced politically by a parliamentary constitution since 1958, which replaced the parliamentary form of government by a semi-presidential one. Both the National Assembly and the President are directly elected under the TRS system of representation. This system of election tends to moderate political pluralization and fragmentation.

The cultural diversely of Sri Lanka is replicated politically by the use of the list proportional representation in the national legislature. The President is elected under the SV system. However, the unitary nature of the constitution has a moderating effect on political diversity.

In terms of party system characteristics, the two presidential systems in our study in this section are different in that the USA has developed a two-party system, whereas Brazil has got a multi-party system. Both the semi-presidential systems here – France and Sri Lanka – have evolved into multi-party systems of polarized pluralism in terms of Giovanni Sartori’s (1976:131-145) typology of party systems.

We will discuss each of these party systems with special reference to coalition governments in turn. A point of clarification is in order here, however. Presidential systems, especially with two-party systems, preclude coalition governments in the sense in which we have been discussing the term in the foregoing. For coalition government is by definition a multi-party affair, barring the two parties in a bi-party system joining hands in a crisis or national emergency. Even in that eventuality, the solitary nature of the presidency forecloses a coalition government, unless the president himself is elected by a bi-partisan electoral platform. This is especially true of the USA where there is a long-established tradition of a two-party system of the Democratic Party and the Republican Party or their predecessors. Moreover, the US President is not constitutionally constrained to select his/her ministers from the Congress nor is the cabinet collectively dependent on the majority of the House of Representatives. In multi-party presidential systems, such for example as Brazil, the President may probably be elected by a multi-party coalitional electoral platform, and the President even otherwise elected on a single party platform may appoint a multi-party cabinet. The President in Brazil, incidentally, must appoint members of the cabinet from amongst the members of the Congress. In semi-presidential systems there is a greater probability of a Prime Minister heading a coalition government, especially if such a system is characterized by a multi-party system. Both France and Sri Lanka in this study happen to be characterized by multi-party systems.
The American two-party system comprising the Democratic Party and the Republican Party is more consistently bi-partisan both historically and spatially than the party system in any other country of the world. The two major parties generally account for all the Presidents and almost all the Congressmen bicamerally. But the formal two-party mould of the American politics conceals an extremely pluralistic and regionally diverse political universe nation-wide, both federally and regionally. There are different sets of presidential and congressional party systems. This diversity is also replicated at the state level. So also at the local level. The three strata of party networks and organizations are not organizationally or hierarchically integrated beyond a formal and minimal sense, resulting in a situation in which higher level leadership has practically no control over party leaders down the line. Thus, the American parties are uniquely decentralized in organizational terms. Parties are also marked by low cohesion in the legislative chambers and weak discipline in falling in line behind the presidential policies and strategies even among the party cohorts of the person in the White House. These characteristics of the American parties may be understood sociologically in terms of the “Frontier spirit” in American political culture historically and exceptional economic prosperity and greater equality in industrial and post-industrial America as compared to the rest of the world. These features of American parties are also a product of a constitutional design marked by the principles of separation of powers among the three major organs of governments horizontally and division of powers between the federal and state governments vertically. An exceptionally complex institutional setting of checks and balances is the outcome of this type of constitutional engineering.

The enterprise of government and governance in such a context demands a continuous process of making coalitions across the executive and the legislative branches and among federal and state governments. These shifting coalitions are imperative to break the institutional and policy deadlocks. As Austin Ranney (2004: 773) aptly observes:

“The main coalition builders have included public officials of all kinds, including presidents and their chief political aides in the Cabinet and the Executive Office of the President; members of Congress and their professional staffs; political heads and permanent civil servants in the executive departments and independent agencies; and federal judges and their clerks”.

Ranney goes on to say:
“At least as active and often as powerful as these inside players are the outside players, especially the lobbyists representing the major organized interest groups that feel they have major stakes in the policy outcomes”.

The process has winners and losers, but the diverse and complex institutional landscapes offers opportunities to those who lose in one site to turn to other sites, including finally to the courts.

With a more or less similar presidential-federal constitution, if coupled with political instability, the task of presidential and congressional coalition building in Brazil is also compelling and inescapable, especially when the country is not ruled by a military dictatorship. The point is illustrated by the experience of President Luis Inacio Lula da Silva whose Workers’ Party won a landslide victory in the presidential election of October, 2002. Despite his great personal popularity, Lula’s party could only win less than 20 per cent of total seats in the National Congress and only 14 of 81 seats in the Senate. The party won the election in only three of the lesser states out of the 26. However, President Lula, an ex-union leader, through an appropriate economic policy and pragmatic political strategy has been able to build workable political coalitions bridging his party’s left wing and the conservative political forces in the country (Costa 2005: 99-102).

Despite attempts in the past by a military regime to introduce two-party systems by legal fiat (Bamgbose 2008), Nigerian party system continues to be a multi-partisan dispensation. The 2007 presidential election was contested by 18 parties, though Umare Yar’Aduba of People’s Democratic Party registered 69.82 per cent of votes, with the runner up Mohannadu Buhari of All Nigeria People’s Party trailing behind with 18.72 %. Parliamentary elections for the House Representatives and the Senate (both directly electable) also featured the same two parties as the winner and the runner-up, among five other parties. As in the case of the USA, the informal coalition-building across organs and level of governments in Nigeria falls mainly on the president and the leaders of the legislative branch as well as on the governors. However, federal democracy in Nigeria has still a long way to go. Commenting on the recent political dynamics in the country, Nze (2005: 235) raises the question “Whether inter-party competition is being replaced by the emergence of one ‘super party’ and intra party competition.”

The 1999 constitution in Nigeria dispensed with the earlier parliamentary federal arrangement and adopted a presidential-federal dispensation complete with separation of
powers among the legislative executive, and judicial organs of governments and the division of powers between the federal and state governments with residual powers left with the latter.

Despite attempts in the past by a military regime to introduce a two-party system by legal fiat (Bamgbose 2008), Nigerian party system continues to be a multi-partisan dispensation. The 2007 presidential election was contested by 18 parties, though Umaru Yar’Aduba of People’s Democratic Party registered 69.82 per cent of vote, with the runner up Mohammadu Buhari of All Nigeria People’s Party trailing behind with 18.72 per cent. Parliamentary elections for the House Representatives and the Senate (both directly electable) also featured the same two parties as the winner and the runner-up, among five other parties. As in the case of the USA, the informal coalition-building across organs and levels governments in Nigeria falls mainly on the President and the leaders of the legislative branch as well as on the Governors. However, federal democracy in Nigeria has still a long way to go. Commenting on the recent political dynamics in the country, Nze (2005:235) raises the question as to “whether inter-party competition is being replaced by emergence of one ‘super party’ and intra-party competition”?

Despite the absence of major cultural contradictions and the electoral system of the Fifth Republic that simplifies political divisions by plurality-majority representation as well as run-off presidential elections that polarize the winner and runner-up, France has been endowed with a fragmented and fractionated multi-party system. This is presumably the effect of the revolutionary tradition and penchant for popular sovereignty. The political spectrum is divided among the right and centre, far right, and left. Unlike several other West European countries, the social democratic political forces on the left are not that strong and united in France. The main parties today are the Rally for the Republic (RPR) and the Union for French Democracy (UDF) on the right, the National Front (FN) on the far right, the Socialist Party (PS), and the French Communist Party (PCF) on the left. The rise of the far right National Front is a development since the mid-1980s. Its influence waned since 1998, but it got a shot in the arm in 2002.

The RPR is a direct inheritor of the Gaullist party of Charles De Gaulle, the founder of the Fifth Republic in 1958. From 1958 to 1975, the Gaullists controlled both the presidency and the premiership. 1986 marked a political as well as economic turning point in French politics. The year witnessed the routinization of charismatic nationalist right-wing domination of the republic and transition to a more competitive politics under divided governments (with the presidency and prime ministership controlled by different
sets of parties) and “cohabitation” of the President and the Prime Minister, in other words, coalition between the head of the state and the head of the government. It was also in 1986 that the government embraced neoliberal economic reforms and initiated privatization of nationalized industries.

The French political system displays a complex pattern of triple coalitions: firstly, among the parties of the right-centre, left (socialists, communists, and Greens), and far right (FN/MNR) in electoral politics; secondly, among party families joining a government; and thirdly, the cohabitation coalition between the President and the Prime Minister.

During the concordant common control of the Presidency and the government by the winning coalition of parties, the French system “resembled that of the cabinet in a presidential regime such as the United States, rather than that of a government in a parliamentary system such as Britain and the earlier French republics” (Schain 2004: 244). The relationship in the double-headed executive changes during periods of cohabitation (from 1986 to 1988, between 1993 and 1995, and between 1997 and 2002). During these periods either a conservative majority controlled parliament and the President was a socialist, or the parliament was controlled by the left and the President was from a conservative party. During such periods of cohabitation, the President tends to “occupy the foreground in foreign and military affairs, in accordance with his interpretation of his mandate under the constitution” and the Prime Minister becomes “the effective leader of the executive and pursue[s] government objectives, but avoids interfering with presidential prerogatives” (Schain 2004: 245).

The multi-party system in Sri Lanka has made coalitional formations among parties necessary for both the presidential and the parliamentary elections. For example, the 2005 presidential election was contested by 13 coalitional or single party candidates, but only two contestants accounted for 98.72 per cent of votes. These were Mahinda Rajpakse of the United People's Freedom Alliance (50.29 per cent ) and Ranil Wickremesinghe of the United National Party (48.43 per cent ). The 2004 parliamentary election was contested by three coalitions of parties and a large number of other coalitions and parties. The 8-party United People's Freedom Alliance won the polls with 45.60 per cent of votes and 46.67 per cent of seats. The 2-party United National Front got 37.83 per cent of votes and (36.44 per cent of seats, trailed by the 4-party Tamil National Alliance (Illankai Tamil Arasu Katchi) with 6.84 per cent of votes and 9.78 per cent seats. Only four other parties or alliances got more than one seat in the unicameral Parliament, ranging between 9 to 1 seats. Both the President and the Prime Minister thus came from the same coalition
of parties, i.e. United People’s Freedom Alliance. The multi-party system of the country has been dominated by the socialist Sri Lanka Freedom Party (SLFP) and the conservative United National Party (UNP), both subscribing to democracy, encouragement to Sinhalese culture, and nonalignment in international relations. The party system includes anti-systemic organizations like the separatist Liberation Tiger Tamil Eelam (LTTE) in the northern and eastern provinces widely assumed to be proxied in the Parliament by the Tamil National Alliance. Another such party is the Sinhalese ethnic Janatha Vimukthi Peramuna (JVP) which was behind both of Sri Lanka’s southern insurgencies in the 1970s and 1980s. It has become established as a mainstream party and is currently part of the ruling UPFA coalition.

There have been proposals to abolish the semi-presidential constitution in Sri Lanka and go back to the parliamentary system. With the Tamil separatist movement leading to the emergency and civil war since 1983 having been militarily crushed in 2009, these proposals may perhaps be seriously taken up and implemented along with the devolutionary scheme under the 13th constitutional amendment suspended in a limbo for long. Sri Lanka has survived “the destructive effects of prolonged ethnic conflict” and “it remains a functioning democracy and one of the few postcolonial states with an unbroken record of democratic rule” (De Silva 1997). The challenge of devolutionary and eventually federal democracy and multicultural and multi-party coalitional governance made messy by intolerance and majoritarianism reflected both in the government and the opposition since the 1970s still lies ahead. The developing coalitional framework of governance augurs well for the consolidation of democracy in the country.

Part VI

Concluding Observations

Like democracy and federalism generally coalitional governance may not be the most stable and effective form of rule, but it is more representative and accountable, other factors being the same. This point hardly needs an elaboration as an institutionalized multi-party coalitional framework of government, especially in a federal context, is a device of consensual rather than majoritarian governance. Almost by definition, a coalition situation “dictates an accommodative politics of compromise and conciliation in which smaller parties and less powerful interests potentially get to have a say in government and public policy. A greater part of the electorate can get representation in government than [had] been typical in India, where all Congress majority governments [had] won a majority
of seats on the basis of only a plurality of votes, the collective majority of voters thus finding themselves unrepresented in government” (Sridharan 1997:2). However, this greater representativeness of coalition governments is maximized under proportional representation system. Under single-member constituency plurality or first-past-the-post representation law, the vote-seat share disproportionality invariably reduces the greater representativeness of coalition governments “primarily with regard to legislatures and only distantly to the electorate and society at large” (Sridharan 1997:2). However, the complex diversities of India blunt the supposed effect of plurality electoral system on the number of parties. India since 1989 has thus been witness to the emergence of a multi-party system even without a proportional representation system.

For reasons of stability and flexibility of operation, national political and administrative elites and top industrialists prefer single-party majority governments to coalition governments. Majority one-party governments are also considered the norm in Anglo-American-influenced and British Commonwealth political systems, and coalition governments are seen as an aberration and a passing phase. Yet single-party majority governments are not always available on wish list, and coalition governments are a much more recurrent feature in these polities than they may appear prima facie. This much is clear from the survey of these political systems in the foregoing parts of this paper. Practically all Commonwealth parliamentary-federal systems have had at least some phases of coalitional governance. A typical Commonwealth model of such political systems may be said to be marked by a multicultural and/or multinational society, plurality-majority representation system, a multi-party system with federal coalitional governance, and constitutional courts with the power of judicial review, in some cases tending to judicial activism.

Western Europe is almost unique in the most widely prevalent use of proportional representation, multi-party systems, coalition governments, direct democracy or at any rate referendum, principle of parliamentary supremacy and Kelsenian constitutional courts, and supranational confederal institutions of the European Union (EU) including the European charter of rights and the European Court of Justice whose case law is commonly honoured by national courts despite national judicial sensibilities especially in the United Kingdom. A large majority of EU member-states have also joined the Euro currency and the Schenzen visa system. There are a European Parliament, a European Council, and a European Commission. If the Lisbon Treaty is ratified by a few remaining 27 member-states, pretty soon there will be the European President and Foreign Minister. All in all,
Europe offers a new model of government and governance, in which the culture of coalitional and consensual political decision making has become institutionalized nationally and supranationally.

In our selected comparative study of some Asian parliamentary systems (Japan, Israel, and Nepal), some presidential systems (the USA, Brazil and Nigeria), and some semi-presidential systems (France and Sri Lanka), we find that inter-party parliamentary coalition governments, presidential-congressional coalition-building, and President-Prime Minister cohabitation are the basic stuff of the enterprise of government and governance, the latter going beyond the formal structures of government.

The case against coalition government premised on instability and its dialatory and ineffective nature cannot also be accepted at its face value. It must be subjected to discursive scrutiny and empirical investigation. A decisive and effective government that leads to overcentralization or systematic exclusion of some regions or communities or their under-representation in the power structure may in the long run lead to political instability of much more disastrous consequences than mere governmental instability that can be more easily managed or compensated by structural or functional substitutes, e.g. bureaucracy, independent regulatory authorities, judicialization of politics, etc.

Traditionally considered unstable, recent studies of coalition governments in comparative settings have shown that this is not necessarily true of all types of coalition governments. Kaare Strom (1987: 109) observes: “Minimal winning coalitions exhibit substantially greater stability than minority coalitions and oversized governments, and can prove as stable as single-party governments”. Evidence from India is also differential and complex. While large and heterogeneous coalition governments in Indian states between 1967-71 were very unstable, the Communist Party of India (Marxist)-led left front coalition governments in West Bengal, Kerala, and Tripura since 1977 have been remarkably stable. So have been the Congress-led United Democratic Front governments in Kerala since the late 1970s. The early federal coalition governments led by Janata Dal since 1989 in India were extremely unstable. However, the Congress minority government headed by P.V. Narasimha Rao (1991-1996), the Bharatiya Janata Party-led National Democratic Alliance government led by Atal Bihari Vajpayee (1999-2004), and the Congress-led United Progressive Alliance government steered by Manmohan Singh and Sonia Gandhi (2004-2009) creditably completed their five-year mandates. The last mentioned government was reelected in 2009 with reinforced electoral strength, and in
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All probability will be stable. However, if the problem of party system fragmentation continues and worsens, Verney (2008) proposes party system reforms through incentives to smaller parties to coalesce into federative national parties via inter-state alliances of smaller parties, as discussed earlier.

This exploration of the theory and practice of coalition and/or minority governments in comparative as well as Indian perspectives suggests that oversize and ideologically incoherent/opportunistic parliamentary coalition governments (support from outside) have a high probability of instability. Executive coalition governments (parties extending parliamentary support plus directly joining the government) have a somewhat greater likelihood of stability. Optimum size, substantive programmatic consensus, and procedural agreement as to the “Dos” and “Don’ts” are some essential prerequisites of durable political and governmental coalitions. Formal coalition pacts negotiated in details in terms of policy issues and mutual obligations have contributed to considerable durability of coalition governments in Germany and Scandinavian countries. “The European model of coalition pacts,” writes Sridharan (1997-20), “tends to implicitly assume clearly articulated party positions along the ideological spectrum as well as agreements (among the non-communist parties, at least) on the fundamentals of the political system”. New Zealand offers additional evidence in favour of formal coalitional pacts. The Indian experience, at least better and evolved parts of it, does not contradict this experience.

Besides the usual dissatisfaction of coalition governments on account of delays and ineffectiveness of government, the first flush of federal coalition governments in India have thrown up two other institutional concerns. These are instability and lack of proper reconciliation between the parliamentary and federal principles of government underlying the constitutional scheme. Early on, the practice of government in India showed that parliamentary component of the government with a prime ministerial (rather than Cabinet) domination overshadowed, rather stifled, the federal parts of the constitution. Since the 1990s, things have gone to the other extreme, i.e. the federal forces have practically undermined the autonomy of the parliamentary wing. This effect, rather distortion, has resulted due to the decline of the previously dominant or majority Congress Party and the failure of other national parties to grow to the majority mark, plus the rise of powerful and often opportunistic regional parties demanding their pound of flesh for their balancing support to make up a majority in the Lok Sabha. The casualty have been the cabinet cohesion, the authority of the Prime Minister crucial for initiation and
coordination of policies, individual responsibility of ministers to the Prime Minister and collective responsibility of the cabinet to the Lok Sabha. This collective responsibility is stretched beyond to the powerful regional satraps who stay in state politics, nominate their protégés over the head of the Prime Minister and remote-control them. Coalition partners in the government try to build “empires” in the ministries parceled out to them. This tendency undermines the autonomy and integrity of parliamentary government. Both the state governments and the Union government are entitled to enjoy autonomy from each other under the Indian parliamentary-federal constitution.
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