Chapter I

INTRODUCTION
India has emerged as a fast growing economy during the recent period. Economists like Kuznets, Colin Clark and Fisher are of the view that occupational structure undergoes a change along with economic growth of a country. As the economy progresses, labour and capital have a tendency to shift from primary to secondary and ultimately to tertiary sector. In other words, process of economic development is invariably associated with a significant shift in the concentration of employment and investment from primary to secondary and tertiary sectors. In India, still 59.2 per cent of the population depends on the primary sector, i.e., agriculture. The government buoyed in its revenue and also is conscious of the fact that the nation is still home to the largest number of destituted.

The incidence of poverty was high in rural areas as compared to the urban areas of the country. High incidence of rural poverty has been a major problem faced by the Indian economy since independence. According to the Suresh D Tendulkar Committee Report, which is submitted in November 2009, the estimates of poverty ratio for rural and urban areas of the country for 2004-05 were 41.80 per cent and 25.70 per cent respectively and that for the entire country it was 37.20 per cent. So, it is expected

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3 Ibid, p.579.
from a democratic State like India to have a Governance model where redistribution and equity is adhered to as far as possible. Government in that context will have to have that 'last mile connectivity' so as to bring the fruits of the development to the proverbial 'last man' in the queue.

Being primarily an agricultural economy as far as the number of people engaged in that domain is concerned; the aforesaid 'last man' resides in the villages. India is a land of villages where there are 6,40,867 villages according to 2011 Census of the Government of India. Out of the total of 1210.2 million population in India according to 2011 Census, the size of rural population is 833.1 million (68.84 per cent of the total population).5

The late Prime Minister Rajiv Gandhi had openly admitted that there was a huge leakage in the delivery system of the government programmes and of every rupee spent by the government on anti-poverty programmes, only 15 paise reached the intended beneficiaries.6 The only way to reach to that village who is dispossessed and do not even think himself to be part and parcel of this economy is to make him an active stakeholder. This could be done by making the whole concept of Governance imbibe into the virtues of 'bottom-up' approach.

The present conditions, particularly in the developing countries, demonstrate that the state and the government are no longer effective and capable of serving the people and ensuring good governance. One finds a

wide gap between the citizens and the government. Governments, by their unlimited expansion and growth, have come to take away a major chunk of the revenues as management cost to deliver services. In the process of expansion, people have been driven away from governance and participation in the development process. To perform the above task, steps have been taken to devolve powers from the federal government to the lowest unit of administration in the society.

By giving power to the villager, they will become aware, active and responsible. 'Village democracy' is that model of Governance that makes the principles of democracy percolate to the 'last man'. Henceforth, inclusivity can only come from making the Panchayati Raj Institutions also called the three-tier of Governance (after the Union and the provincial government) politically dynamic and economically self-sustainable. With only inclusivity in governance, the fruits of financial inclusion can be sustainably 'harvested'. India can take legitimate pride in creating the world's biggest infrastructure of elected rural self-government institutions in the form of the three-tier Panchayati Raj.

1.1 Concept of Gram Panchayat (GP)

The word "Panchayat" literally means "assembly" (ayat) of five (panch) wise and respected elders chosen and accepted by the local community. However, there are different forms of assemblies. Traditionally, these assemblies settled disputes between individuals and villages. Modern
Indian government has decentralized several administrative functions to the local level, empowering elected Gram Panchayats⁷.

Mahatma Gandhi, the Father of the Nation of India, viewed that 'the Panchayat is the executive body of Gram Sabha to provide civic facilities to the people in its jurisdiction. Indian independence must begin at the bottom. Thus, every village will be a republic of Panchayat, having full powers⁸.

The Indian village is the smallest composite and self-sustained unit of social, cultural, economic and administrative organization in rural areas of the country. It has clear-cut physical boundary markers demarcated by natural objects like tree, river, stream or hill etc. and a particular type of social composition of the community. A village comprises of resources like land (private agriculture land, common land), water (pond, well, irrigation system, both traditional and/or modern), grassland and forest (community owned or government – owned).

According to the Census definition, a village represents a parcel of land, the boundaries of which are defined and settled by revenue survey. It may, but need not always necessarily be, a single house cluster marking its distinctiveness as a residential locality⁹.

⁷ http://en.wikipedia.org/wiki/Panchayati_raj
All the villages have not Panchayats as some of them are very small. This is why some villages which are very small are clubbed to make a Panchayat. A village or a group of villages with a population not less than 500 is declared as a Panchayat village. Every Panchayat village has a Gram Panchayat duly notified by the Government. The Government can however relax the condition pertaining to the required minimum population if it so wishes. However, the reason(s) for introducing change in the condition must be duly recorded in writing\textsuperscript{10}. There are approximately 250,000 Gram Panchayats in India, each of which serves an average population of 5000. Gram Panchayats vary substantially from state to state\textsuperscript{11}.

Panchayat Village is the entity where the primary unit at the local level of the Panchayati Raj Institutions (PRI) becomes operational in India. At a local level, there are three hierarchies, namely, Gram Panchayats, blocks and districts. Gram Panchayats are the lowest tier in the local administrative framework and may be responsible for one or more villages or habitations\textsuperscript{12}. The Gram Panchayats or the Village Panchayats are the local government bodies in India\textsuperscript{13}. Gram Panchayats have the power to make bylaws and constitute statutory bodies with responsibility for handling government funds, collecting revenue and delegating responsibilities\textsuperscript{14}. The

\textsuperscript{10} Ibid, p.29.

\textsuperscript{11} Mahesh Chandra Chaturvedi (2012), \textit{op. cit.}

\textsuperscript{12} Mahesh Chandra Chaturvedi (2012), 'India's Waters, Environment, Economy and Development', Taylor & Francis Group, CRC Press, New York, USA, p.74.

\textsuperscript{13} Om Gupta (2006), 'Encyclopaedia of India, Pakistan and Bangladesh', Isha Books, Delhi, p.835.

\textsuperscript{14} Mahesh Chandra Chaturvedi (2012), \textit{op. cit.}
Gram Panchayat is an executive organ of the village government. Its main functions are managing the local affairs and promoting village development with the help of available local resources and with the government assistance, both financial and technical\textsuperscript{15}. 

The Panchayat is called by different names in different States of India. It is named Panchayat in Andhra Pradesh, Tamil Nadu, Maharashtra and Rajasthan, the Gram Panchayat in Punjab, Bihar, Karnataka, Madhya Pradesh and the Gaon Panchayat in Assam, Gujarat, Uttar Pradesh, etc.\textsuperscript{16}

The village is divided into 'wards' for electing members of the Gram Panchayat. The Gram Panchayat consists of the elected Sarpach, who is head of the Gram Panchayat and an Up-Sarpanch (Vice-President), who is also elected. Each Gram Panchayat also has a Secretary, who may service one or more Gram Panchayats. The Gram Sabha is a general body of electors, whereas the Gram Panchayat is an executive, elected body. The executive has to perform its duties as per directed given by the general body\textsuperscript{17}. Gram Panchayats in every state has its own characteristics and even election procedures to these institutions are at variance.

\textsuperscript{15}Goel, S.L., Shalini Rajneesh (2009), \textit{op. cit.}, p.130.

\textsuperscript{16}\textit{Ibid.}

1.2 Genesis of Panchayati Raj Institutions

The Panchayati Raj is a South Asian political system mainly in India, Pakistan, and Nepal. It is actually the oldest system of local government in the Indian subcontinent. Panchayats have been the backbone of the Indian villages since the beginning of the recorded history. They have been a vibrant and dynamic identity of the Indian villages. It is an age-old indigenous Indian politico-administrative institution. It owes its origin to the different traditional patterns of governance, in the phases of history, in many parts of India. Being associated with the Indian culture and heritage, the Panchayat bodies have been working for the Indian villagers, in some form or other, since ancient times. Villages have been playing pivotal role in the Indian life through the ages and so also the different types of Panchayat bodies18.

It is believed that the concept of self-governance existed during Rig Vedic period (around 1200 B.C.). There were ‘Village Sabhas’ and Gramins (Assemblies of Village elders) who took interest in the welfare of villages. The system of Panchayati Raj is thus deeply rooted in our tradition. From time immemorial, this system has exercised powers, both executive and judicial. This village government took decisions and actions based upon religious values and customs and traditional conventions with respect to

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various matters. The Indian Panchayati Raj has been developed on the basis of traditional society and polity of India with a vedic approach.

Prior to the British rule, the villages of India were self-sufficient. But, the British changed this by neglecting the villages and concentrating on the development of the cities for their own benefit. After independence, affairs at the local level have been entrusted to the local representatives. In India, it is a centralized move, and not based on the demand from below, to decentralize powers to the grassroots. There is absolutely no movement of the people to takeover power. People have demands and the Government has no mechanism to meet the demands of the people. There is a gap between the people and the Government. There are conscious efforts on the part of the Government to bridge the gap between the people and the Government. Decentralization of powers has several objectives of which the principal one is bringing people closer to the Government and making people participate in governance. Decentralization is popular and holds many promises.

The genesis of the present system of Panchayati Raj can be traced back to the vision of Mahatma Gandhi, who advocated the revival of the traditional Panchayats so that Gram Swaraj, which had been an integral part of the social system of India, could become a reality. Gandhiji expounded his ideas on Gram Swaraj (Village republics) in the Harijan (a

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19 Goel, S.L., Shalini Rajneesh (2009), op. cit., p.5.
20 Pratap Chandra Swain (2008), op. cit.
21 Palanithurai G (2005), 'Building skills and capability among Gram Panchayat Presidents – An experience from the field', Concept Publishing Company, New Delhi, pp.6-7.
The Panchayat for him was an instrument which would foster peoples’ participation in the governance of the country. Gandhiji had spoken of a village republic in which the government would be annually elected by adult villagers and which would have the authority and jurisdiction in the fields of legislation, judiciary and executive decision making without interference from the state government. Gandhiji saw Panchayats as a perfect democracy based upon individual freedom.

Gandhiji’s vision of Gram Swaraj (village republics) was first shattered when in their wisdom our constitution makers put Panchayati Raj in the directive principles of the constitution, merely saying that the state shall take steps to organize village Panchayats with powers to function as units of self-government.

After Independence the subject of local Government was allotted to state list of functions. Article 40 of the Constitution of India says, “the State should take steps to organize village Panchayats and endow them with such power and authority as may be necessary to enable them to function as units of self-government.” Since then, the Local Government in India entered into a new phase.

Under List II of the Seventh Schedule of the Constitution, that is the State List, “Local Government, that is to say, the constitution and powers of

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23 Ibid.

municipal corporations, improvement trusts, district boards, mining settlement authorities and local authorities for the purpose of local self-government of village administration" was to remain the domain of States. In respect of matters in the State List, according to article 246 of the Constitution, the State concerned has exclusive powers to make laws. Accordingly, measures were taken by States to bring their laws in conformity with Article 40 of the Constitution. In those States, where no law was existing to provide for Panchayats, new laws were passed. By 1951-52, there were over 70,000 village Panchayats functioning in the country25.

The emphasis on rural development in the country started with the introduction of Community Development (C.D.) projects in 1952 and National Extension Service (NES) subsequently. The community development projects were expected to motivate the rural people to undertake self-reliantly community based approach for the improvement of economic and social conditions of their life and environment. With the passage of time the original Community Development Programmes bogged down with bureaucratic rules. People by and large remained uninvolved and the desired development efforts were not made. Community Development Programme had not succeeded in evoking the response needed from the

people. Development analysts traced the failure of Community Development Project to the absence of people's participation among other reasons\textsuperscript{26}.

The Government of India constituted a team known as “Committee on Plan Projects” with Balwantray Mehta, as its Chairman. The Balwantrai Mehta study team’s report (1957) was a critical turning point. It recommended the establishment of statutory elective local bodies. The Committee recommended the setting up of a three tier structure of Panchayati Raj to expedite development efforts and to change local participation. This belated realization paved the way for the first Panchayati Raj\textsuperscript{27}.

On 2\textsuperscript{nd} October 1959, Jawaharlal Nehru, former Prime Minister of India (1947-1964), had inaugurated Panchayati Raj at a national rally in Naguar in Rajasthan. The period between 1959 and 1964 can be described as the golden period of the first generation Panchayati Raj Institutions. By the mid-sixties, Panchayats had emerged in most parts of the country and there was over 2,17,300 village Panchayats covering 96 per cent of the 5,79,000 inhabited villages and 92 per cent of the rural population. On an average, a Panchayat covered a population of about 2,400, in two to three villages\textsuperscript{28}. At present, there are 6,40,867 villages according to 2011 Census.

\textsuperscript{27} Johari, J.C., (2004), Indian Polity’, Lotus Press, New Delhi, pp.138-142.
After Jawaharlal Nehru’s death, political leaders were determined to end the threat to their leadership from the village, mandal or district leadership. They paid only lip service to local self-government. The bureaucracy, in alliance with local powers, state and central-level politicians, began to discredit the new system by highlighting its shortcomings. For about thirteen years, from 1964 to 1977, Panchayati Raj remained the whipping boy of all those who wanted to discredit the decentralization of power. Elections were either not held or were frequently postponed. In most cases, these bodies were superseded.

The appointment of the Asoka Mehta Committee in 1977 marked a turning point in the concepts and practices of Panchayati Raj. The Asoka Mehta Committee was set up to enquire into the working of the Panchayati Raj Institutions and to suggest measures to strengthen them so as to enable a decentralized system of planning and development to be effective. The Committee’s report (1978) is a seminal document to make Panchayats ‘an organic, integral part of our democratic process’. The Panchayati Raj Institutions which came into being in certain states after the Asoka Mehta Committee’s recommendations could be considered the second generation Panchayats. The second generation of Panchayati Raj Institutions can be said to have started when the West Bengal government took the initiative in 1978 to give new life to its Panchayats on the lines of he Asoka Mehta Committee’s recommendations. The most important thrust of the second phase was that the Panchayats emerged from a development organization at

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29 Ibid, p.15.
the local level into a political institution. The emphasis shifted from the bureaucracy to the political elements. The Balwantrai Mehta study team had made development central to the Panchayat system, while in Bengal, Karnataka, Andhra Pradesh, and later in Jammu and Kashmir following the Asoka Mehta Committee Report, the attempt had been to make Panchayats into genuine political institutions. Thus they were a microcosm of the state itself.\(^{30}\)

### 1.2 Constitutional support

It is well established that constitutional support and legislative measures are necessary for bringing about social change. There was no constitutional support for self-government below the state level till April 1993. A three-dimensional approach — political will, people’s awareness, and building healthy conventions and traditions under girded by constitutional and legislative measures is a must for any far-reaching changes to be brought about in our society, and when one of these is weak the entire measure may remain in form and without content. There was a growing realization that it was lack of constitutional support that had led to the sad state of affairs of the Panchayats. State governments could not establish full-fledged Panchayati Raj without adequate constitutional safeguards. Asok Mehta Committee made the first official recommendation for including Panchayati Raj in the constitution in keeping with its approach.

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that Panchayats should be regarded as political rather than were developmental institutions.31

Rajiv Gandhi, former Prime Minister of India (1984-1989), opined that "the third level of democracy, i.e., at the Panchayat level, is weak and it affects the first and second levels of democracy which are governed from Delhi and the State capitals, because people at the top level have become paper tigers and the structure has become hollow. This has to be set right by strengthening the Panchayati Raj Institutions. To strengthen our democracy in Delhi and in the State capitals, it is essential to strengthen the democratic Institutions at the Panchayat level. To gear up the development process, it is necessary to strengthen the Panchayati Raj Institutions at district, block and village levels."32 Hence, Rajiv Gandhi introduced the 64th and the 65th Constitution Amendment Bills in the Lok Sabha in 1989. The bills are passed in the Lok Sabha and were not adopted in the Rajya Sabha. Later, P.V. Narasimha Rao, former Prime Minister of India (1991-1996), took initiative to pass these bills. The two bills were passed during his government and became the 73rd and the 74th Constitution Amendment Acts of 1992, which are now, placed in Part IX and Part IX A of the Constitution. Thus, almost after five decades of Independence, the Government of India revolutionized the concept of decentralization of power through the Constitution (73rd Amendment) Act, 1992 by making Panchayati Raj institutions as a part of the constitution.

31 Ibid, pp.9-10.
1.2.1 73rd Amendment to the Constitution

Although sporadic attempts were made in India to devolve greater powers to rural and urban local bodies, the impetus gathered momentum only after the 73rd and 74th Constitutional amendments. As stated earlier, constitutional changes to empower the Panchayati Raj Institutions were carried out through 73rd Constitutional Amendment Ac, 1992 which was passed by the Parliament and came into operation with effect from April 25, 1993. It conferred Constitutional status to Panchayati Raj Institutions and accorded them durability, continuity, and financial viability. Provisions were made for due representation of weaker sections of the society, and regular and periodic elections. Since then the government became a three tiers systems, say, centre, state and local. The main features of the 73rd Amendment Act are the following:

- Constitution of a three tier structure of Panchayats in every state (at village, intermediate and district levels) having a population of twenty lakhs (Article 243 B).
- Reservation of seats for scheduled castes, scheduled tribes, and women (Article 243 D).
- Fixed tenure for Panchayat bodies (Article 243E).
- Transfer of powers, authority and responsibilities to Panchayats, including 29 subjects listed in the Eleventh Schedule (Article 243 G).
- Powers to impose taxes (Article 243 H).

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The 73rd Constitution Amendment Act empowers the State Legislatures to make laws for the organization of Panchayats at the village level as well as at the higher levels of a district. Such laws shall define the mode of composition, strength of the members including reservation of seats for Scheduled Castes, Scheduled Tribes and other weaker sections of the community. The members shall be elected directly by the voters of the territorial constituencies, but the law of the State shall lay down the method of the inclusion of the MPs and MLAs of that area in such bodies and the representation of the Chairpersons of such bodies at the intermediate or higher levels of Panchayati Raj in a district. Every village will have a Grama Sabha comprising of all the registered voters in the Panchayat area.

The Chairperson of a village Panchayat shall be elected directly by the voters of a constituency, but the law of the State government shall determine the method of the election of the Chairpersons of higher units of Panchayati Raj in a district. The law of the State Government shall also provide for reservation of seats for Scheduled Castes (excluding Arunachal Pradesh) and Scheduled Tribes in proportion to their population in the State, but 1/3 seats shall be reserved for women under such a category. The reservation system shall come to an end if the provision for such reservations, as given in Article 334 of the Indian constitution, comes to an end.

Every Panchayat shall have a uniform five year term and election to constitute new bodies shall be completed before the expiry of the term. In the event of dissolution, election should be compulsorily held within six
months. Every state shall constitute state election commission to conduct election for local bodies.

The State legislatures may also make a law to:

a) authorise a Panchayat to levy, collect and appropriate such taxes, duties, tolls and fees in accordance with such procedure and subject to such limits;

b) assign to a Panchayat such taxes, duties, tolls and fees levied and collected by the State Government for such purposes and subject to such conditions and limits;

c) provide for making such grants-in-aid to the Panchayat from the consolidated fund of the State and

d) provide for constitution of such funds for crediting all moneys received respectively by or on behalf of the Panchayats, and also for the withdrawal of such money there from, as may be specified in the law.

However, the most important features of this arrangement is related to financial autonomy granted to such bodies. Within one year of the commencement of this Amendment Act and thereafter at the expiration of every fifth year, the Governor shall have the power to set up a Finance Commission to review the financial position of the Panchayats and to make recommendations to the Government as (a) to the principles which shall govern (i) the distribution between the State and the Panchayats of the net
proceeds of the taxes, duties, tolls and fees leviable by the State, which may be divided between them under this part and the allocation between the Panchayats of all levels of their respective shares of such proceeds, (ii) the determination of the taxes, duties, tolls and fees which may be assigned to or appropriated by the Panchayats, (iii) the grants-in-aid to the Panchayats from the Consolidated Fund of the State; (b) any other matter referred to the Finance Commission by the Governor in the interest of sound finance of the Panchayats. The composition, jurisdiction and the procedure of working of the Finance Commission shall be determined by the law of the State. It shall submit its report to the Governor who shall cause it to the laid before the State legislature together with an explanatory memorandum as to the action taken thereon. The State Legislature shall also make law for the maintenance of accounts of these bodies under the superintendence, direction and control of the Chief Electoral Officer of the State.

The State Legislatures may make laws for the conferment of such powers and authority on these bodies as may be necessary to enable them to function as units of self-government and such a law may contain provision for the devolution of powers and responsibilities upon Panchayats at the appropriate level, subject to such conditions as may be specified there under, with respect to – (i) the preparation of the plans for economic development and social justice and (ii) the implementation of schemes for economic development and social justice as may be entrusted to them including those in relating to the matters listed in Schedule XI of the Constitution.

In accordance with 73rd constitutional amendment Act 1992, all State Government implemented three-tier Panchayati Raj system. All the States passed their acts before 24 April 1994 in conformity with the 73rd Amendment. The operationalization of the principles varies from State to
State. The States have also appointed state election commissions and finance commissions. However, experts feel that in many cases the States have not lived up to the expectations of the people in giving powers to the three tiers of Panchayats. In other words, they have tried to follow the letter of the amendment and not its spirit.

1.3 Evolution of Gram Panchayat Finances

There is fiscal decentralization to rural local government in India. The concept of Panchayats as local self-government has its origin since the days of the British regime. Lord Ripon's resolution on local self government in the year 1882 laid special stress on the importance of entrusting to the local boards, not merely the expenditure of fixed allotment of funds, but the management of certain local sources of revenue. The review of administration of Local Boards held in 1897 exhibited the sources from which the revenue of local boards was being derived in different provinces. The major sources of income as found in this review include land revenue, provincial grants, different local receipts, say, cattle pound receipts, educational receipts, medical receipts, miscellaneous receipts, receipts from civil works and contributions etc. The largest item of revenue was the land revenue. The miscellaneous receipts head included such items like sale proceeds of trees, recoveries of the cost of collecting road cess arrears etc. After this review, the major recommendation that came in the British period for the development of the Panchayat system was laid down in the


Government of India Resolution in the year 1918. As regards the powers of taxation in rural boards, it is found from the resolution that 'where no limit has been imposed by the law on the rate of the cess, a change in the rate at which the cess is levied will need the sanction of outside authority; but where a limit is imposed, either by existing or by future legislation, a rural board will be at liberty to vary the rate at which the cess is levied within the limits imposed by law without the interference of outside authority'. Beside giving liberty to the local boards, the Government of India Resolution, 1918 endorsed the recommendation made by the Royal Commission on Decentralization, 1909 that the system of obligation to the local bodies to devote fixed portion of their revenues to particulars items of expenditure should be done away with, so as to give these bodies liberty to act\textsuperscript{36}.

Later, it was found from the survey made by the India Statutory Commission on Local Self Governance, 1928 that financial resources are generally quite inadequate in local self governments due to reluctance of the selected members to impose local tax. After much experimentation in the British period, the independent India constituted a committee, namely, Local Finance Enquiry Committee in the year 1950 to recommend the ways and means of improving the conditions of the financial resources of the local bodies. The Committee observed that the reluctance of local bodies to make use of their existing financial powers and resources to the fullest extent and to impose taxation even when the need for such a step was clearly admitted

\textsuperscript{36} Sujit Kumar Dutta, Dilip Kumar Ghosh (2006), \textit{Institutions for Development – The Case of Panchayats}, Mittal Publications, New Delhi, pp.73-88.
was the main factor for chronic want of funds by the local bodies\(^{37}\). In 1951, the Local Finance Enquiry Committee studied this problem and recommended unconditional assignment of 15 per cent of land revenue raised in the Panchayat area and the proceeds of the surcharge levied on the transfer of immovable property to the Panchayats. Panchayats were also to be empowered to raise their own resources by levying certain taxes in their territories.

In 1954, the Taxation Enquiry Committee recommended for reserving certain taxes such as taxes on land and building, octroi, tax on non-mechanical transport, tax on property, tax on profession, tax on advertisement other than newspapers, theater tax, duty on transfer of property etc. for Panchayats\(^{38}\).

Later, the Government of India constituted a Study team under the Chairmanship of Balwantrai Mehta to study community projects and National Extension Service in 1957. The Committee reported that the collection of Panchayat taxes is generally not satisfactory. The Committee noticed lukewarm attitude of the functionaries in collecting the taxes. The Committee recommended a list of sources of income to be assigned to local bodies. Further, the Committee recommended imposing tax on professionals, trades, callings and employment levied by the Panchayat Samity, and surcharge on duty on the transfer of immovable property. Rents and profits accruing from properties like ferries, fisheries etc. within

\(^{37}\) Ibid.

the jurisdiction of the Panchayats, constructed and maintained by the Panchayats. The net proceeds of tolls and leases on roads and bridges etc. in the Panchayats are transferred to the Panchayats. Pilgrim tax could be imposed. Tax on entertainments, amusements, etc. should be imposed. Primary education cess be imposed. Proceeds from periodical fairs and markets, bazaars, hats and shanties where the frequency of such holding invariably should for more than once in a month irrespective of the place where it was being hold. A share of motor vehicle taxes should be transferred. Grants made by the government and public contributions given voluntarily are another source of income. Further, the Committee recommended adequate flow of grants-in-aid from the State governments to these bodies.

Moreover, the sources suggested by the Mehta Committee included items like (i) property or house tax, (ii) tax in daily, bi-weekly or weekly markets, bazaars, hats or shanties irrespective of their location, (iii) tax on carriages, carts, bicycles, rickshaws, boats and pack animals, (iv) Octroi or terminal tax, (v) conservancy tax, (vi) Water and lighting rate, (vii) Income from cattle pounds, (viii) Fees to be charged for the registration of animals sold within the local area of the Panchayat for the purpose of slaughter house, sairs, etc., and (ix) Grants from the Panchayat samitis.

Next to say is the Santhanam Committee. The Government of India constituted a study team under the Chairmanship of K. Santhanam to study

39 Ibid.
40 Ibid.
resources and finances of Panchayati Raj Institutions in 1962. The Santhanam Committee Report, the all-India report on Panchayat finances published as far back as 1963, clearly brought out the need for financial and administrative autonomy as well as an integrated policy to build self-governing institutions at the sub-state level\textsuperscript{41}. Further, it is recommended that one of the fundamental requirements of Panchayati Raj Institutions is that adequate resources should be available to the Panchayati Raj Institutions through transfer or otherwise, to enable them to discharge their responsibilities.

It is also suggested that the resources can be broadly classified as follows – resources transferred in the form of grants and loans by Central and State Governments, by higher tiers of Panchayati Raj to the lower tiers, the proceeds of taxes, duties, cesses etc, which the institutions can levy under their own powers, income from remunerative assets developed by these institutions and gifts and donations from public spirited citizens and voluntary contributions by the people. Further, Committee made an effort to classify the resources of the Panchayats into five items, viz., (i). proceeds from different taxes levied by the Panchayat bodies, (ii). Fees and charges imposed, (iii). Income from property, investments and remunerative undertakings of the Panchayats, (iv). Grants/assistances received from the State Governments and (v). Contributions from the public\textsuperscript{42}.


\textsuperscript{42} Sujit Kumar Dutta, Dilip Kumar Ghosh (2006), \textit{op. cit.}
The Committee felt that though taxation is undoubtedly an unpleasant task but at least a few compulsory taxes is essential. House tax, profession tax and vehicle tax are suitable for this purpose. Further, there should be minimum and maximum limits of tax rates. In considering vehicle tax, the Committee recommended to exempt motor vehicles as they are subject to special taxation laws. The committee preferred to include all bullock carts, bicycles and other vehicles under this vehicle tax.43

The Committee classified fees and rates into three categories, namely, fees for services, license fees and fees in the nature of fines and penalties. Fees for services include fees for water supply, drainage, street lighting and conservancy. License fees include license fees for registration of cattle sold, collection of hides and skins, tea stalls and restaurants or goods exposed for sell in markets, for direction of new buildings for use of common land and community property and for carrying an offensive or dangerous trade. Fees in the nature of fines and penalties could be levied by Panchayat for (i) encroachments, (ii). failure to take licenses and (iii) unauthorized possession of or dealing in prohibited articles, etc.44

In addition to the sources of income mentioned, the grant from the State was the major source of support for the Panchayats. The Committee classified the assistance from the State Governments to the Panchayati Raj Institutions into three broad categories, namely, share of taxes and statutory grants, grants and loans for plan and other development schemes

43 Ibid.
44 Ibid.
and grants and subventions for non plan purposes such as maintenance of staff and institutions, matching, equalization and deficit grants\textsuperscript{45}.

After the Santhanam Committee, the major discussions on financial resources of the Panchayats were taken place in ‘Asoka Mehta Committee (1978)’. This Committee also observed that there was general reluctance by the Panchayat bodies to impose taxes. This reluctance was not only visible in the grass root tier but also persisted in the upper tiers. To pursue the matter of building up own sources, Asoka Mehta Committee recommended that some taxes should be made binding on the Panchayats. The Committee recommended that certain taxes like house tax, profession tax, entertainment tax, special taxes on land and buildings and certain fees like various market fees should be levied compulsorily by the Panchayati Raj Institutions at the appropriate level. For augmenting the resource base of the Panchayats, the Committee recommended that the periodic revision of taxes would help in increasing the resources of the Panchayati Raj Institutions. Further, it is also recommended that remunerative enterprises be undertaken by the Panchayats to increase employment opportunities in the respective area and improve their own financial resources. Assigned revenue constituted important elements of financial resources of the Panchayats. Assigned revenue includes land revenue, cesses in land revenues and surcharge on stamp duties. In addition to sharing in tax and

\textsuperscript{45} Ibid.
cess, grants from the State Governments are also a major source of income of the Panchayats\textsuperscript{46}.

About eight years later, in 1986, the Singhvi Committee among others, suggested pattern of compulsory and optional levies and a list of subjects in respect of which powers to levy taxes and fees may be entrusted to Panchayati Raj Institutions with a provision that for a given period, the State governments shall levy and collect on behalf of Panchayati Raj Institutions and shall disburse to them, on the basis of the recommendations of the finance commission in each state\textsuperscript{47}.

On the basis of the recommendations of the various committees mentioned above, the State Governments have made provisions in their respective Panchayati Raj Acts. To ensure that its scheme is properly implemented, the 73rd Amendments also mandate the establishment of a Finance Commission by each State, every fifth year, to assess the financial position of the Panchayats and to make recommendations\textsuperscript{48}.

A new Article 243H was incorporated in the Constitution through the Constitution (Seventy Third Amendment) Act, 1992 with the caption 'Power to impose taxes by and funds of the Panchayats'.

\textsuperscript{46} Ibid.


\textsuperscript{48} Ibid.
The Legislature of a State may, by law:

(a) authorize a Panchayat to levy, collect and appropriate such taxes, duties, tolls and fees in accordance with such procedure and subject to such limits;

(b) assign to a Panchayat such taxes, duties, tolls and fees levied and collected by the State Government for such purposes and subject to such conditions and limits;

(c) provide for making such grants in aid to the Panchayats from the consolidated fund of the State; and

(d) provide for constitution of such funds for crediting all moneys received respectively, by or on behalf of the Panchayats and also for the withdrawals of such money therefore, as may be specified in the law.

In addition to this Article 243H, the Seventy Third Amendment to the Constitution incorporated a new Article 243I, where provision was made for constitution of Finance Commission in each State for reviewing the financial position of the Panchayat bodies and determining the principles for sharing funds (both tax and grant in aid) between the State and the Panchayat bodies. The fiscal decentralization envisaged in the Constitutional Amendment has the potential to significantly improve the efficiency of public services delivery in the country. With the passage of the Seventy third Amendment Act, 1992, the States also brought in changes in their respective Panchayat Acts. Therefore, Panchayats can levy taxes prescribed
In the three-tier Panchayati Raj system, only Gram Panchayats are empowered to levy taxes. Panchayati Raj statutes of each of the State contain a detailed list of taxes and their rates which Panchayats may levy. Schedule XI of the Indian Constitution defines the functional items for which States may devolve responsibility to Panchayats. While States vary in the extent to which they devolve policy powers to the Gram Panchayat, most Gram Panchayats have responsibilities of civic administration in the village together with limited independent taxation powers.

1.4 Structure of Gram Panchayat Finances

The resources of the Panchayats broadly comprise internal revenue mobilized by themselves through the exercise of tax and non-tax powers, and resources received from the state in the form of devolution and grant from both the state and the Union governments. There are essentially three type of taxes which devolve on Panchayats. They are own taxes – the levy, collection and use of which vests in the Panchayats by the Statue; assigned taxes – the levy and collection of which vests in the State but its use vests in the Panchayats; and shared taxes, the levy and collection of which vests in the state government but shares with local bodies. The non-tax sources for

Panchayati Raj Institutions consist of revenues from license fees, fines and penalties, rent/leases on governmental properties.

The resources of Panchayati Raj bodies during the first two decades of Panchayati Raj Institutions in India may be grouped under four broad heads, say, (i). own sources, (ii). assigned revenues, (3). Grants, and (4) loans. Own resources consist principally of taxes and fees, non-tax revenues including income from remunerative enterprises and contribution from the public. The most important taxes levied in different states by the Panchayats broadly are house tax, profession tax, vehicle tax, tax on agricultural land, pilgrim tax, entertainment tax, tax on animals and the like. Taxes and fees accounted for about one – third of the total income of Gram Panchayats during the early periods. On average, roughly 10 per cent of a GP’s total revenue comes from own revenues, with the remainder consisting of transfers from higher levels of government.

In addition to the powers of taxation enjoyed by the different tiers of PRIs and the revenues collected from various non-tax sources, state legislations provided for the sharing of certain taxes levied and collected by the State governments. Land revenue, cesses on land revenue and surcharge on stamp duty were the principal assigned taxes distributed between the PRIs. Some states like Kerala had given the entire land revenue to Gram Panchayats. Despite several other sources of income, grants from state governments happened to be the single major source of income for the

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Panchayati Raj bodies. Most prominent grants were establishment grants, incentive grants, matching grants and equalization grants. The establishment grants were given to meet administrative expenses especially those arising as a result of the transfer of personnel by certain state governments to PR bodies. The incentive grants were meant to give incentives for unanimous election of Sarpanch, agricultural production, collection of taxes etc. The potential of incentives in the form of matching grants have provided incentives to the PRIs to adequately tap the existing tax paying potential of the rural people\textsuperscript{54}. Apart from taxes, non-tax revenues and grants, some Panchayats have relied on loans also to promote development works\textsuperscript{55}. Donations and voluntary contributions are also the sources of Gram Panchayats.

The taxes, duties, tolls and fees to be levied by the Panchayats and assigned to them and grant-in-aid to be given to them are left to the discretion of the state governments. Therefore the fiscal mismatch not only between own revenue and total expenditure but also between total revenue and total expenditure of Panchayats. Hence, Panchayats are facing a huge deficit and their own sources are meager to meet out emerging fiscal need and even meeting out the committed liabilities.

1.5 Statement of the problem

Finance constitutes the backbone, the life and blood of Governments as it provides fuel to the administrative machinery. The importance of

\textsuperscript{54} Ibid, p.7.

\textsuperscript{55} Ibid, p.8.
finance is so great in administration that David Lloyd George, former Prime Minister of the United Kingdom (1916-1922), is said to have once remarked that 'Government is finance'.

The local self-government institutions have their own course of action, planning for it and funding it independently. The Panchayati Raj bodies shoulder a wide range of responsibilities. There are about 29 functions enlisted in the Eleventh Schedule of the Constitution for which the responsibility has been given to the Panchayati Raj Institutions. Out of these, 21 functions are mainly devoted to the developmental activities and social responsibilities. For these essential objectives to be realized, it is necessary that they should have their own sources of finance which should be assured of sources and not depend on donations and like grants-in-aid. The local government system in India had been weakened mainly because of financial inadequacy and lack of financial autonomy.

Finances should follow functional assignments. But Panchayats are marked by their poor internal revenue effort and high dependence on grants-in-aid and assigned revenues from both Central and State governments. Improving own sources strengthen the link between revenue and expenditure decisions of the rural local bodies at the margin, which is extremely important to promote both efficiency and accountability in the provision of services. But the resource mobilization by the Panchayats is

limited as the taxes like land revenue, house tax, etc. transferred to them by the State governments are less buoyant in nature.

Further, expenditure functions remain non-transparent and very little expenditure autonomy has been given. It is important to specify expenditure responsibilities to enhance accountability, reduce unproductive overlap, duplication of authority and legal challenges. As state governments faced themselves with several resource constraints, the revenue accruals to the local bodies are not adequate to enable them to effectively deliver the required standards of public services.

Gram Panchayat is the rural local body at bottom level of Panchayati Raj that is expected to perform a number of civic and developmental activities facing inadequacy of funds on one side and taking away of tax levying powers of Gram Panchayats by State Government on the other side. Panchayati Raj system is a novel experiment in the history of rural local-government, in which, Gram Panchayat plays a vital role in decentralized development of India. But it is unfortunate to note that Gram Panchayats in the country are not developed due to lack of proper monitoring of its revenues and expenditures. Further, the experience of democratic decentralization of power varies from country to country and, in India, from province to province. It varies extensively even among districts. Historical study of the local government is also an important factor in assessing their efficiency in providing local needs\(^57\). While Constitutional Amendment has

led to a marginal improvement in rural public service delivery, it is apparent that much more needs to be done to provide even a basic level of services to all the rural population.

While recent studies on Panchayati Raj Institutions (PRIs) in India have focused on issues relating to the role of Panchayats in poverty alleviation and employment generation programmes, resource allocation favouring disadvantaged groups and improved participation of women in decision-making process, the own revenue effort of Panchayats has received little attention. There is no standing national database on Panchayat finances in India, which limits any meaningful analysis of revenue effort of Panchayats. Reports of the central finance commissions serve as the only source of information. Central finance commissions collect data on own revenue of Panchayats from the state governments. The Eleventh Finance Commission (EFC) Report provides data on own revenue of the PRIs for the period 1990-91 to 1997-98, which was further extended by the Twelfth Finance Commission (TFC) Report up to 2002-03. However, the data reported by the successive Central Finance Commissions are not comparable. There are very few studies on the Gram Panchayat finances. No study is taken up so far to examine the pattern of imposition and collection of taxes over a period of time by the Gram Panchayats besides expenditures in Andhra Pradesh in particular. To understand the Gram Panchayat finances, detailed study is an imperative.

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Against this background, there is a need to conduct a study to examine these issues. Therefore, the present study is taken up to examine these issues. The present study is unique as it studies the revenues and expenditures of Gram Panchayats over a period of 30 years in the three selected districts of Andhra Pradesh and offers policy implications to improve the financial administration of the Gram Panchayats.

1.6 Importance of the study

Panchayat Raj offers enormous possibilities of making local governance and the rural development process more need-based, participatory and productive, while at the same time being accountable and transparent. The actual operation of PRIs is of greater significance now more than ever before. PRIs are considered as partners of the central and state governments in carrying out development functions. Article 243-G introduced by the 73rd amendment to the Constitution empowers state governments to vest village Panchayats with powers and responsibilities to prepare plans for their economic development and social justice and implement schemes to achieve these objectives. PRIs are also seen as a vehicle to implement major development programmes. Consequently, there is a continuous effort on the part of policy-makers to evolve systems and mechanisms to enable PRIs to perform and deliver their newer roles more effectively.

Provision of services responding to local needs and preferences in a decentralised government system depends to a large extent upon the willingness and ability of the local governments to raise revenue from their
own sources. To bring about the direct and willing participation of the villagers in development, the planning process has to start from the village. Panchayati Raj institutions were expected to give the lead in this matter. The major objective of devolving revenue raising powers to the PRIs is to enable them to function as effective institutions of self-government at local level by improving their autonomy in planning and decision-making.

One of the key tests to real empowerment of Panchayats lies in the ability of local self-governing institutions to finance their own expenditures through internal generation of resources. Addressing the fundamental issues surrounding Panchayat finances is central to improving the ability of Gram Panchayats to fulfil their role as agents of economic development. Focused action on internal revenue generation by Panchayats could have a transformative effect on local governance and, more fundamentally, the quality of life of citizens in rural India. In view of the magnitude and nature of development activities entrusted to Panchayats, it is impossible for them to raise revenue locally to meet all the expenditures. Even if adequate tax resources are devolved, the Panchayats do not have the machinery to administer them. To know the problems involved in the Panchayat finances a detailed enquiry is needed regarding all sources of revenue of the Panchayats and their expenditures. Hence, studies are needed to suggest measures to improve the revenue generation of the Gram Panchayats. Therefore the present study will be useful to the policy makers, researchers, academicians, etc.
1.7 Objectives of the Study

Keeping in view of the importance of the study, the objectives of the study are:

i. To examine the Panchayati Raj system in Andhra Pradesh.

ii. To examine the trends in revenues and expenditures of the sample Gram Panchayats over a period of 30 years.

iii. To examine the pattern of imposition of taxes and collection of taxes by the sample Gram Panchayats

iv. To analyze the pattern of expenditure of the sample Gram Panchayats

v. To suggest policy implications in order to frame the financial structure of Gram Panchayats on sound economic lines.

1.8 Methodology

The study is conducted in Andhra Pradesh state of India. Andhra Pradesh is divided into three regions, namely, Coastal Andhra, Rayalaseema and Telangana regions. Multi-stage random sampling method is used while selecting the sample. In the first stage, One district is selected randomly from each region. Next, One Mandal is selected from each of the selected district. Later, three Gram Panchayats are selected randomly from each of the selected Mandal. Thus, the sample size of the present study is nine Gram Panchayats. The sample distribution is given in Table – 1.1.
### Table 1.1

Table showing the Sample *Gram Panchayats* of Sample Districts in Andhra Pradesh

<table>
<thead>
<tr>
<th>Sl. No.</th>
<th>Region</th>
<th>Sample Districts</th>
<th>Sample Gram Panchayats</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Andhra Region</td>
<td>Guntur</td>
<td>1. Dachepalli</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>2. Kesanupalli</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>3. Gamalapadu</td>
</tr>
<tr>
<td>2</td>
<td>Rayalaseema Region</td>
<td>Kurnool</td>
<td>1. Koilakuntala</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>2. Boyalakuntala</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>3. Chapirevula</td>
</tr>
<tr>
<td>3</td>
<td>Telangana Region</td>
<td>Warangal</td>
<td>1. Nekkonda</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>2. Chandragonda</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>3. Dekhakunta</td>
</tr>
<tr>
<td>Total</td>
<td>3</td>
<td>9</td>
<td></td>
</tr>
</tbody>
</table>

The present study used both primary and secondary data. Most of the data used in this study is secondary data, which is collected from official records of concerned *Gram Panchayats* and Mandal Parishads and Mandal Revenue Offices. Data has also been collected from audited reports of *Gram Panchayats*, bank passbooks etc., in certain villages. Substantial part of the thesis is based on secondary data. The collected data has been processed through Statistical Package for Social Sciences (SPSS) Software. Primary data regarding payment of taxes is collected through discussions with the Villagers and Panchayat Staff.

### 1.8.1 Statistical Tools used for Analysis

Simple statistical tools - averages and percentages are used to compare various items of income and expenditures. In order to estimate the relative change, index numbers are used by taking 1980-81 as fixed base year in most of the cases.
Estimation of Trend

There are various econometric methods that can be used to derive estimates of the parameters of economic relationship from statistical observations. However, the mechanics of least-squares are simple to understand.

Assuming two variables, X and Y the functional relationship may be written as:

\[ Y = f(X) \]

where

\[ X = \text{Explanatory variable} \]
\[ Y = \text{Dependent variable} \]

We further assume that the variables are related with the simplest possible mathematical form, that is, the relationship between these two variables is linear of the form

\[ Y_i = b_0 + b_1 X_i \]

This form implies that there is one-way causation between the variables Y and X. The parameters, \( b_0 \) and \( b_1 \) are estimated using the 'normal' equations of OLS

\[ \sum Y_i = nb_0 + b_1 \sum X_i \]
\[ \sum X_iY_i = b^0 \sum X_i + b_1 \sum X_i^2 \]

Since sampling errors are inevitable in all estimates, it is necessary to measure the size of the error and determine the degree of confidence in the validity of the estimates. In this regard, the 'standard error test' is popular and the same is applied in this study. This helps us to decide whether the estimates \( b_0 \) and \( b_1 \) are significantly different from zero, i.e., whether the sample from which they have been estimated might have come from a population whose true parameters are zero \( (b_0 = 0 \text{ and/or } b_1 = 0) \).

The square of the correlation coefficient, \( R^2 \) is used for judging the explanatory power of the linear regression of \( Y \) on \( X \). A measure of the goodness of fit is the square of the correlation coefficient \( R^2 \) which shows the percentage of the total variation of the dependent variable that can be explained by the independent variable \( X \).

1.9 Scope of the Present Study

The present study is strictly confined to the finances of Gram Panchayats in Andhra Pradesh. It is an attempt for detailed investigation of Gram Panchayat finances over a period of 30 years i.e., from 1980-81 to 2009-2010. In view of several constraints in selecting census method, sampling technique is used in this study. This study covers Nine Gram Panchayats from three districts covering Coastal Andhra, Rayalaseema and Telangana regions of Andhra Pradesh.

It became very difficult to collect the required data in the case of some variables because of several reasons like improper book keeping, record
maintenance etc. On some occasions it is inevitable to go through the bank passbooks for getting the revenues and expenditures in certain villages. As such, necessary adjustments were also made in the available data to suit the totals, wherever necessary.

Despite all these limitations, earnest efforts were made to collect reliable and appropriate data from the available sources. The same data is used effectively to draw conclusions and to give appropriate suggestions for the effective financial administration of Gram Panchayats.

1.10 Organization of the study

The study is presented in seven Chapters. Introduction is given in Chapter I. Chapter II provides review of literature. Study area profile is presented in Chapter III. Panchayati Raj System in Andhra Pradesh is discussed in Chapter IV. Analysis of revenues of the sample Gram Panchayats is presented in Chapter V. Chapter VI details expenditures of the sample Gram Panchayats. The study and its implications are enumerated in the last Chapter.