CHAPTER IV

CONSTITUTIONAL AND EXTRA-CONSTITUTIONAL AGENCIES
FOR MAKING FISCAL ADJUSTMENTS

INTRODUCTION

The most difficult problem of Federalism is that of dividing a satisfactory distribution of fiscal resources between the Central and Regional Governments. Asok Chanda has rightly pointed out 'in no Federation has it been possible to provide for allocation of resources to correspond with the allocation of functions'. Even if initially an equitable distribution is arrived at, with the passage of time and change in economic system, it tends to disturb equilibrium. In a Federation, there is always a yawning gap between the growing functions and State's own resources, which has become an inherent feature of all established Federations. Thus, there is always a need to have a machinery for periodical review of the financial disequilibrium and some flexible balancing devices for effecting adjustments in 'Federal Financial Relations'.

We had noticed in Chapter III, that the Constitution of India had made an elaborate division of taxing powers


of Union and States. However, the financial powers placed at the disposal of the Union are enormous, while the States had been assigned inelastic or eroding sources of revenue. The division of taxing power has made the dependence of the States to the Union nearly absolute. Despite the elaborate distribution of sources of revenue between the Union and the States, it was clear to the framers of the Constitution that the scheme embodied in the Constitution would work to the disadvantage of the States. In this regard concern was repeatedly voiced in the Constituent Assembly. K. Santhanam complained 'the Provinces would be beggars at the door of the Centre'. H. N. Kunzru felt that 'emergency powers would lead to the financial autocracy of the Centre'. While Biswanath Das expressed the fear that the States might be treated 'as charity boys of the North Block of the Secretariat'. The Constitution of India, has, however, followed the efficiency criteria in the devolution of resources between the Union and States which resulted into assigning the qualitatively superior resources to Union and stagnant

6. Ibid., Vol. IX at 508.
7. Ibid., at 207.
There exists every possibility of imbalance between revenue needs and actual receipts from assigned taxes. Therefore, it was felt that unless provisions to balance disequilibrium were made, a mere devolution of resources of revenue between the Union and States might stereotype the existing economic disparities between the States as such. It was realised that no distribution, however, carefully drawn could be satisfactory at all times and for all circumstances. The Constitution makers realised that 'Union-State Financial Relations' is a recurring problem and like other Federations, in India too, there was a need for flexible balancing devices for effecting adjustments in 'Federal Financial Relations'. 'The problem of Federal finance', says Gadgil, 'is thus that of maintaining through changing circumstances needed correspondence between functions and resources without the use of any coercive power'. Thus the framers after providing for the taxes which Centre shall share or may share with the Provinces and fiscal need grants from the Centre to the States, desisted from laying down any rigid formula to


determine the specific amounts payable to the States by the Centre under each head. So that States autonomy is not impaired it was provided that quantum of such devolution of funds and principles of their distribution shall be left entirely to an independent and impartial agency which would access the changing needs of the States and take into account the imbalances between the rich and poor States in making the recommendations. In India, the Finance Commission as a Constitutional agency, Planning Commission, National Development Council and Union Ministries especially the Finance Ministry, non-Constitutional agencies play a vital role in making Federal fiscal adjustments.

The present chapter is devoted to a discussion on the origin, composition, powers and functions of both constitutional and non-constitutional agencies which are working in making fiscal adjustments between Union and States. The role of these agencies in transfer of resources had been discussed at length in the subsequent chapters at the appropriate places.

(A) **Finance Commission - A Constitutional Agency**

The Finance Commission enjoys a unique position in the Indian Constitution as there is no other agency comparable to it in any of the earlier Federations. With a view to avoid frequent political pressures to which the Parliament and Cabinet are subject, the study of financial relations by an independent body has been provided in the Constitution. Such a body helps in the adjustment of fiscal relations according to circumstances. Moreover, the reconciliation of Federal control and regional autonomy and of Federal financial interests with State financial requirements can be achieved only if there is an independent body to deal with. In the following pages, an attempt is made to make an indepth study of the Finance Commission.

(1) **Origin of Finance Commission**

We can trace back the origin of our Finance Commission to the period when British Government used to obtain expert administrative advice before formulating a public policy or drafting a legislation. While suggesting

for an independent and impartial body like the Finance Commission, to review and advice on Federal Financial Relations in India, the makers of our Constitution were greatly influenced by the Financial Relations Committee appointed by the then British Government headed by Lord Meston in 1919, Indian Taxation Enquiry Committee (1925), First Peel Committee (1931), Second Peel Committee (1932), Parry Committee (1932) and the Joint Parliamentary Committee on Indian Constitutional Reform. While debating on Article 280 in the Constituent Assembly, the Constitutional Advisor, B.N. Rau, described it 'as a quasi-judicial body whose functions are to do justice between the States'. Dr. Ambedkar also agreed with B.N. Rau's views. T.T. Krishnamachari pleaded that the purpose of setting up of Finance Commission is to assure States that they will have a fair deal. At the time of framing the Constitution, the makers had before them Commonwealth Grants Commission in Australian Federation created in 1933 which annually examines the pleas of the claimant units for Commonwealth assistance. This Commission was created by an Act of Parliament. They had also in view the recommendation of Canadian Royal Commission on Dominion Provincial Relations,

to establish a body to advise the Dominion Government on National Adjustment Grants', but this recommendation was not accepted.

However, it seems that our Constitution-makers were influenced by the existence of Commonwealth Grants Commission of Australian Federation and therefore, they also provided for an independent body named 'Finance Commission' in Indian Constitution. The Rajamanner Committee on Centre-State Relations was of the similar view when it stated that the idea appeared to have been mooted by West Bengal in its memorandum to the Expert Committee on the Financial Provisions. West Bengal had emphasised the need for a Finance Commission on the lines of the Commonwealth Grants Commission in Australia.

(ii) Appointment and Composition of Finance Commission

Article 280 of the Constitution provides for creating an important and independent body named Finance Commission.

Commission. This Article empowers the President to appoint the Commission within 2 years from the date of commencement of the Constitution and thereafter at the expiry of every fifth year or at such earlier time as the President might consider necessary. Originally, the Finance Commission was to constitute of five members in all, one Chairman and four other members appointed by the President. The Constitution empowered the Parliament to prescribe by law the manner of their selection and requisite qualifications. Parliament while exercising this power had enacted the Finance Commission (Miscellaneous Provisions) Act 1961. The Act provided that the Chairman is to be selected from amongst persons who have had experience in public affairs and its members should be persons who:

(a) are or have been or are qualified to be appointed as judges of a High Court; or
(b) have special knowledge of the finances and accounts of the Government; or
(c) have wide experience in financial matters and in administration; or
(d) have a special knowledge of economics.

20. Constitution of India, Article 280, clause (1).
21. Ibid., clause (2).
23. Ibid., Section 3.
A person of unsound mind, an undischarged insolvent or a convict of an offence amounting to moral turpitude or has financial or other interests prejudicially affecting his functions as a member of the Commission is disqualified to be a member of the Commission. Since the Finance Commission is a temporary body, therefore, the tenure of its members is determined by the President in the order of the appointment. Generally, the members are appointed for a term of one year. The members are to discharge such whole time or part time service as President may specify in each case and their emoluments are determined by Government of India. The members of the Finance Commission are eligible for re-appointment but so far except M.V. Rangachari who was the member of Second and Third Finance Commission and Dr. C.H. Hanumanta Rao, member of Seventh and Eighth Finance Commission, none other had been re-appointed. This Commission has the status and powers of a Civil Court under the Code of Civil Procedure 1908, in the matter of summoning and enforcing the attendance of witnesses, requiring the production of documents and calling for public records from any court or

24. Ibid., Sections 4 and 5.
25. Ibid., Section 6.
26. Ibid., Section 7.
27. Ibid., Section 8.
Similarly, the Commission can ask any person to furnish information on any matter under its consideration and such a person cannot claim protection under section 54(2) of the Indian Income Tax Act 1922 or any other law available to him. Thus the Commission is a Civil Court for all purposes.

Section 480 and 482 of the Criminal Procedure Code, 1898.

(iii) **Functions of Finance Commission**

The functions of the Finance Commission are recommendatory and advisory in nature. The Constitution itself lays down the functions to be performed by the Finance Commission. The Commission is required to make recommendations to the President on the following issues:

(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 principle which should govern the grants

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28. The relevant provision reads: Section 480 "No pleader who practises in the court of any Magistrate shall sit as a Magistrate in that Court or in any Court within the local jurisdiction of that Court".

Section 482 reads: "Nothing in this Code shall be deemed to limit or affect the inherent powers of the High Court to make such orders as may be necessary to give effect to any order under this Code or to prevent abuse of the process of any Court or otherwise to secure the ends of justice."
in aid of the revenues of the State: out of the Consolidated Fund of India.

(c) any other matter referred to the Commission by the President in the interest of sound finance. Under this clause apart from tax sharing and grants in aid the President can refer any other matter to the Commission.

The Constitution had no doubt fixed the terms of reference of the Finance Commission, yet there is an element of flexibility in the terms of reference under sub clause (c) of Article 280(3). Under this sub clause, the President had been given wide power to refer any matter to the Commission, 'in the interest of sound finance'. This sub clause had in fact enlarged the scope of Finance Commission. The terms of reference under Article 280(3)(a) and (b) have been the regular feature of successive Finance Commissions. However, under sub clause (3)(c), the President had been asking the Finance Commissions to give their recommendations on the additional terms of reference. Under the additional terms of reference the Second Finance Commission was asked to make recommendations on the principles governing the distribution of excise duty in respect of property other than agricultural land, modifications if any in the payment of the loan by the States, the
distribution of additional duties of excise and the principles for the distribution of net proceeds of tax on railway fares. Similarly under sub clause (c) the Third Finance Commission was asked to recommend whether any change is to be made in the distribution of excise duty additional excise duty and tax on railway fares. The Fourth Finance Commission was required to make recommendations with regard to principles governing the distribution of excise duty and additional excise duty. The Fifth Finance Commission was required to suggest ways and means for discouraging overdrafts and the methods for exploiting States own resources. The Sixth Finance Commission was required to suggest ways for curtailing States indebtedness problems. The Seventh Finance Commission was to make recommendations for financing the relief expenditure and suggest means for dealing with the non plan capital gap of States. The Eighth Finance Commission in its additional terms of reference was to suggest the scope for raising revenue from the taxes and duties under Article 269. Similarly the

Ninth Finance Commission created in 1987 in its additional terms of reference has been asked to suggest changes if any to be made in the principles governing the distribution of additional duties of excise and grants in lieu of railway passenger fares.

Thus from the study of successive Finance Commissions it becomes clear that the additional terms of reference had also become a regular feature of the Finance Commissions.

(iv) Procedure of Finance Commission

After the appointment of the Commission by the Government of India, the personnel assume charge and initiate the work of the Commission. The procedure which the Finance Commission follows can be discussed under the following three stages:

First stage: In the first stage the Finance Commission writes letters to the Union Ministers, State Governments and the Accountant General for supplying relevant material. The Union Government and the State Governments are asked to submit estimates of their normal expenditure and amounts of revenue


over the next five years. They are also requested to give their views on the existing basis of devolution of taxes and duties. Immediately after receiving replies from the respective governments, the Commission at its level scrutinizes these estimates and calls the concerned officials to Delhi for consultation and seeking clarification in the matter. After the clarifications, the Commission makes these estimates comparable among the States by eliminating abnormal and unusual items.

Second stage: In the second stage, the Commission tours the capital cities of all States and Union Territories and hear the case of each State for financial assistance. As a general rule the Commission hears the Chief Ministers and Finance Minister of the respective States along with their aides. Each State at this stage submits a memorandum, pleading therein for more financial assistance. Generally, the discussion with the State Government is held in camera but the discussions are released to the press through press releases. Besides the respective governments the Commission may meet individuals and associations interested in the matter and hold discussions with them.

Final stage: After the completion of second stage which takes too much time of the Commission, the Commission meets in Delhi for preparing and finalising its report.
After following the above procedure, the Commission finally submits its report to the President of India. The report is submitted few months prior to the month in which Union Budget is presented in the Parliament. The President recommends its consideration and implementation by the Union Cabinet. The Union Cabinet on the advice of Union Finance Ministry decides as to which recommendations are to be accepted and which are not to be accepted. If recommendations are accepted, they will be included in the Union Budget after placing them before Parliament. The Parliament will also legislate laws for the matters contained in Article 270, 272 and 275.

As the recommendations of the Finance Commission are of advisory in nature, therefore, the President is not bound by them. B.N. Rau, the Constitutional Advisor to the Constituent Assembly realised, 'as a matter of strict law, the recommendations of the Finance Commission are mere recommendatory and it is open to the President if he thinks fit to depart from them. But it should be unwise to depart 39 from them except for patent error'. As a matter of practice, the recommendations as made by the successive Finance Commissions had been generally accepted by the President or Parliament as the case may be.

39. Supra note 16 at 383-84.
However, there remains a serious anomaly in the working of Finance Commissions that it entirely depends on the data and information on the financial needs of the States as supplied by the States. Such information may not be wholly correct and incorrect information may be supplied for securing more financial assistance. Moreover the Commission does not publish the details of their estimates of revenue gaps and financial needs of each State which leads to assumption that the Commission tries to avoid criteria of their arbitrary assumptions, estimations and methods etc. by hiding them from the public.

The Finance Commission was intended to be an important tribunal to judge the counter claims of the Union and States. K.R. Bombwall held the view that the provisions of Finance Commission as contained in our Constitution are an innovation of far reaching importance to the working of Indian Federal Finance. Similarly D.T. Lakdawala observed that the Finance Commission is expected to play the role of a wise man, a judge between the conflicting claims of the States on the one hand and the Centre on the other. But

40. Supra note 38.
contrary to the expectations the study of various Finance Commissions reveal that whereas the Union was required to lay down only terms of reference of the Finance Commission, it along with terms of reference had been issuing guidelines for discharging their functions. Thus it is alleged that the Finance Commission has become a tool in the hands of Central Government. However, inspite of its all criticisms, we may regard it as the balancing wheel of Indian Federal finance.

(B) Planning Commission - An Extra Constitutional Agency

Large chunk of Central financial assistance flows to the States through specific purpose grants under Article 282. These grants are called discretionary grants as Centre can not be enforced to provide for these grants. Moreover these grants are outside the purview of Finance Commission. Generally these grants are available for Plan purposes. There are certain plan programmes which fall within the State's sphere such as national extension services, agriculture, fisheries, general and technical education and community development, for the purposes of legislation and administration, but being of all India importance, Centre is always interested in their implementation. Therefore, for promoting States action in these areas, the Centre gives grant as incentives to the States. These grants are mostly given
on the advice of the Planning Commission. Thus through the device of Planning Commission, the Centre can persuade, encourage and pressurize the States to keep within the Plan targets.

(1) Origin of Planning Commission

The Constitution of India apart from Concurrent entry, which provides for 'economic and social planning' does not contain any specific provision relating to Planning Commission. Though the framers of our Constitution were aware of the need for economic planning, they did not integrate explicitly economic planning into the Federal democratic political framework. No doubt the 'social and economic planning' was always in the contemplation of national leaders, yet the reason for not including this important aspect in the Constitution seems to be that the framers left it to the nation to give planning the shape it deemed proper. However, the objective of achieving social, economic and political justice is included in the Preamble of the Constitution and some of the means of achieving social and economic justice are grouped under Directive Principles in the Constitution.

43. Supra note 13 at 265.
44. Supra note 12 at 306.
45. Constitution of India, Seventh Schedule, List III, Entry 20
The importance of planning for carrying out the task of economic and social transformation had come to be emphasised in thirties. We can trace back the origin of planning in India to the year 1938, when the President of Congress Party, Subhash Chander Bose, convened a conference of Provincial Ministers of Industries for considering the future economic development in India. This conference appointed a committee named National Planning Committee with Pt. Nehru as Chairman. The main function of this Committee was to study the various aspects of the national economy and to suggest a coordinated Plan for improving the standard of living of Indian people. In 1941, Government of India appointed a Committee under the chairmanship of Central Commerce Member for suggesting Planning for India. In 1943, the Committee appointed in 1941 was replaced by the Reconstitution Committee of the Cabinet with Governor General as its Chairman. This Committee submitted two reports containing suggestions for raising the living standard of the people of India and ensuring employment for all. Finally, the Advisory Planning Board was appointed in 1946 by Pt. Nehru, then Vice President of Interim Cabinet for reviewing the whole Planning process. Thus both these bodies, National Planning Committee and Advisory Planning Planning Board played an important role in the creation of the

47. Supra note 2 at 260-62.
present Planning Commission. Whereas the National Planning Commission provided the base for setting up a centralised Planning machinery, the Advisory Planning Board in its report devised the model of an official and powerful machinery like the Planning Commission, which should devote its attention to the whole field of development.

During discussion some members of the Board pleaded that the Chairman of the designed body should be a Minister of Cabinet rank without portfolio, whereas others were of the view that it should be totally dis-associated from the vicissitudes of politics. The Board however, recommended that this body must be a non political and non ministerial body purely advisory in character. But this report of the Board could not be worked upon because of changing political developments in India, and the existing economic problems could not be solved. Since Pt. Nehru also favoured Planning in India, and in spirit of Pt. Nehru's wishes, the Economic Programme Committee of All India Congress Committee favoured the setting

49. Ibid., at 24.
51. Minoo Masani, 'More Powers to State or ... The Times of India, July 17 at 1 (1983).
up of a permanent Planning Commission, to aid and advice for implementing the Committee's programmes.

(ii) Setting up of Planning Commission

Keeping in view the Economic Planning Committee's intentions and the past developments which had taken place in the Planning so far, the Government's intention to establish a Planning Commission was announced in the President's Address to Parliament towards the end of January, 1950. The President mentioned, 'the Planning Commission was to be established so that the best use can be made of such resources as we possess for the development of the nation'. The actual announcement of the setting up of the Commission was made by the Central Finance Minister in his Budget speech on February 28, 1950 and accordingly the Planning Commission was established by a Resolution of the Government of India dated March 15, 1950. The Resolution provided, 'the people of India have been conscious of the importance of planned development as a means of

raising country's standard of living. During the last three years, the Centre as well as the Provinces have initiated schemes of development but experience has shown that progress was hampered by the absence of adequate co-ordination and of sufficiently precise information about the availability of resources.\(^{56}\)

(iii) **Composition and Functions of Planning Commission**

As regards the composition of the Commission, the Board had suggested that it should be a small full time Planning Commission consisting between three to five members. However, the Resolution setting up the Commission provided that the Commission shall consist of five members in all. The Prime Minister was to be the Chairman of the Commission and four other members were whole time members. Gradually the size of this Commission enlarged and at one time the number of Ministers associated with the Planning Commission increased to

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57. *Supra* note 48.
58. *Supra* note 54.
even seven. This changed the very character of the Commission as those who were formulating the Plans were also associated with the implementation of the Plans.

The Resolution created a Planning Commission in 1950 as a permanent body of National Planning. It was provided in the Resolution that in view of Directive Principles of State Policy as provided in the Constitution and 'declared objectives of the Government to promote a rapid rise in the standard of living of the people', a Planning Commission was being set up to perform the following functions:

1. To make an assessment of the material, capital and human resources of the country, including technical personnel, and investigate the possibilities of augmenting such of these resources as are found to be deficient in relation to the nation's requirements.

2. to formulate a Plan for the most effective and balanced utilisation of the country's resources.

3. on a determination of priorities, define the stages in which the Plan should be carried and propose the allocation of resources for the due completion of each stage;

4. to indicate the factors which are tending to retard economic development and determine the conditions which in view of the current social and political situation should be established for the successful execution of the Plan.

5. to determine the nature of the machinery which will be necessary for securing the successful implementation of each stage of the Plan in all its aspects;

6. to appraise from time to time the progress achieved in the execution of each stage of the Plan and recommend the adjustments of policy and measures that such appraisal may show to be necessary and

7. to make such interim or ancillary recommendations as appear to it to be appropriate either for facilitating the discharge of the duties assigned to it or on a consideration of the prevailing economic conditions, current policies, measures and development programmes or on an examination of such specific problems as may be referred to it for advice by Central or State Governments.
The Resolution indicated that the Commission would be essentially an advisory body and would make recommendations to the Union Cabinet. The Central and State governments were made responsible for implementing the decisions of the Commission. Thus under the Resolution this Commission was envisaged to be a 'staff agency'.

(iv) Reorganisation of Planning Commission

For a long time the States had been asserting that the Planning Commission is a 'super cabinet', therefore, it was realised that it may be re-organised. For this purpose the Administrative Reforms Commission appointed in 1965 for reviewing the whole administrative machinery of the Central Government was assigned the job to formulate a scheme for its re-organisation. After going through the whole functioning of the Planning Commission, the Administrative Reforms Commission submitted an interim report in 1967 along with the interim report of the Study Team on Machinery for Planning Commission appointed earlier by the Administrative Reforms Commission. On the basis of both these reports the Planning Commission was reconstituted in July 1967. After reconstitution it was provided that the Planning Commission was to consist of five members in all that is one Deputy Chairman and four other members. The Prime Minister was
to be the ex officio Chairman and the Union Finance Minister ex officio member. However, Prime Minister was given authority to invite any Minister for attending the meeting of the Planning Commission. This Commission was to be headed by a full time Deputy Chairman, who was to be a chief executive of the Commission.

Though the Commission is a staff agency which advises in matters of Planning and development yet it is unrealistic to expect that the government will modify or reject the decisions of the Commission, which the senior Ministers including the Prime Minister had approved. The Commission is being criticized by the States for deasing from its role of advisory body and for acquiring the status of 'super economic cabinet' of the country which is close to the Union and imposes its will on the States. However, in spite of the criticism of the functioning of Planning Commission, a study of the working of various Planning Commissions reveals that over the years the Central and State governments have been relying heavily on its advice.


The other extra constitutional agency which plays a vital role in the process of Planning in India is the National Development Council. This agency is deeply connected with the Union State Financial Relations in India. In India, Planning has been unified and comprehensive so far as the Planning deals with the both Centre and State subjects. However, since the Constitution demarcates the functions and powers of both layers of government and guarantees autonomy to the States, therefore, it becomes necessary to obtain full co-operation and consent of the constitutional units in any endeavour of national magnitude like planned development of the country.

(i) Origin and composition of National Development Council

If a Plan is to be a national Plan some machinery had to be devised by which the States could be enabled to participate in the formulation of the Plan and the overall policy underlying it. Official discussion on Planning machinery in Government of India had even in 1949 envisaged the creation

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of some kind of a National Economic Council which could work as an organ of inter governmental co-operation in the economic and social field. The Planning Commission realised the necessity of creating a body of this kind in the last stages of its thinking about the Draft outline of the First Five Year Plan. It, therefore, recommended, 'in a country of the size of India where the States have under the Constitution full autonomy, within their own sphere of activities it is necessary to have a forum such as a National Development Council at which from time to time the Prime Minister of India, Chief Ministers of States can review the working of Planning and its various aspects'. Accordingly on the recommendation of the Planning Commission, the Government of India set up the National Development Council in August 1952 by a Resolution.

The Council when created by the Resolution was to consist of the Prime Minister as Chairman, the Chief Ministers of States as members and the members of the Planning Commission. The Resolution did not accord statutory status to the Council so that it remains flexible and informal.

63. Supra note 55 at 37.
64. The First Five Year Plan - A Draft Outline, Government of India Planning Commission, 253 (1951).
(ii) **Functions of National Development Council**

It was outlined in the Resolution that this Council was to be an advisory and reviewing body and its objectives would be to strengthen and mobilize the effort and resources of the nation in support of the Plan, to promote common economic policies in all vital spheres and to ensure the balanced and rapid development of all parts of the country. Thus the National Development Council according to the Resolution was to be the highest forum for discussing issues connected with the Plan. For achieving the objectives as laid down in the Resolution it was to perform the following functions:

1. to review the working of the national Plan from time to time;

2. to consider important questions of social and economic policy affecting national development and

3. to recommend measures for the achievement of the aims and targets set out in the national Plan; including measures to secure the active participation and co-operation of the people, improve the efficiency of the administrative services ensure the fullest development of the less advanced regions

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and sections of the community and through sacrifice borne equally by all citizens, build up resources for national development.

Pandit Jawaharlal Nehru in the capacity of Chairman of National Development Council enumerated three objectives of the National Development Council. These are:

1. to strengthen and mobilise the efforts and resources of the nation in support of the Plan.
2. to promote common economic policies in all vital spheres.
3. to ensure balanced and rapid development of all parts of the country.

(iii) Re-constitution of National Development Council

It was realised by the late Prime Minister Shri Lal Bahadur Sastri that National Development Council had been ignored and it has not been given due importance at the time of formulating the Plans. It was alleged by the States also that National Development Council had been used to be a 'rubber

stamp' for the decisions already take-n by the Planning Commission. In view of these observations, the Administrative Reforms Commission and its Study Team on Machinery for Planning in their Interim Report had recommended that along with the Planning Commission, the National Development Council may also be modified and reconstituted as it is not working to the satisfaction of the States. Therefore, it was reconstituted in 1967 with a view so that it may be supreme political body for guiding the formulation and implementation of Plans and should become a powerful and effective instrument for ensuring all India support for the Plans.

After its reconstitution its size was enlarged and it was to consist of Prime Minister, all Union Ministers, Chief Ministers of all States and Union Territories and Members of the Planning Commission. Delhi Administration was to be represented in the Council by Lt. Governor and Chief Executive Councillor. This reconstituted Council was to meet twice a year. Its functions were redefined as follows:-

1. to prescribe guidelines for the formulation of the national Plan, including the assessment of resources of the Plan.

2. to consider the national Plan as formulated by the Planning Commission.

3. to consider important questions of social and economic policy affecting national development and

4. to review the working of the Plan from time to time and to recommend such measures as are necessary for achieving the aims and targets set out in the national Plan including measures to secure the active participation and cooperation of the people, improve the efficiency of the administrative services, ensure the fullest development of the community through sacrifice borne equally by all citizens and build up resources for national development.

(iv) Working of National Development Council

National Development Council plays an important role in the formulation of annual and Five Year Plans. The Planning

71. Supra note 69.
Commission consults the National Development Council in the formulation of these Plans. The Commission after preparing a rough draft of the Plan which it prepares in consultation with the Central Ministries, Chief Ministers and State Governments places it before the Union Cabinet for its approval. After such an approval is acquired, the rough draft of the Plan is sent to the Council for its suggestions and modifications if any. After seeking the suggestions of the Council, the Plan is sent to the Union Ministries and State Governments for preliminary instructions. After they submit their Plans to the Commission, the Commission starts the work of integration of the Plans and thus emerges the draft plan. Thereafter, the Commission discusses the size and nature of the Plan with the Union Ministries and State Governments and then the tentative conclusions are placed before the Union Cabinet and if approved by the Cabinet, they are considered by the Commission. At this stage also before finalising the Plan, the Planning Commission takes into account the suggestion of the Council, if any. Finally the final draft is placed before the Parliament and if approved it becomes official Plan. Thus the National Development Council is the highest forum for frank and full discussion between the Union and State Governments on issue of national importance.
While appreciating the working of National Development Council Dr. Paras Diwan holds the view that National Development Council is a Federal body which softens the totalitarian aspect of the Planning and makes it cooperative endeavour. Pt. Nehru was of the view that National Development Council was an essential forum for intimate cooperation between Centre and States for all tasks of national development. Similarly K. Santhanam has described it as a 'super cabinet of the entire Indian Federation, a Cabinet functioning for the Governments of Centre and States.

H.M. Patel was also of the similar view when he observed that National Development Council is indeed a policy making body and its decisions cannot be regarded as advisory suggestions.

On the other hand Mr. H.K. Paranjape while criticising the role of National Development Council has stated that it has become too casual spasmodic and almost perfunctory to

72. Supra note 70 at 27.
73. Supra note 67.
74. Union State Relations in India, 47 (1960)
75. Ex-Finance Secretary to the Government of India, Review Section of Indian Journal of Public Administration, October-December at 460 (1959).
ensure that the States participation in the Planning process is either continuous or deep. Likewise the Administrative Reforms Commission has stated that National Development Council has become a forum for ventilation of individual grievances rather than collective discussions of principles and policy. Similarly the Opposition parties in their Srinagar Convention adopted a Resolution stating that National Development Council intended to be the highest policy making body on social and economic issues has functioned in a manner entirely vitiating its original role.

No doubt the National Development Council is the highest representative body of Centre and States in the field of Planning whose approval is obtained before Plan is presented in Parliament, yet it has been functioning more by fits and starts than as a regular element in the Planning process. But with the coming of different political parties into power in the States, the council is becoming an effective tool for exerting pressure over the Centre. This is a praise

worthy development in the field of Planning.

(D) **Union Ministries - Extra Constitutional Agencies**

In addition to the above referred financial assistance as flows through Finance Commission and Planning Commission, the States also get substantial part of assistance in the form of loans or grants from the Central Ministries. These transfers are called 'discretionary transfers' or 'other transfers' as these are not covered either by the recommendations of Finance Commission or Planning Commission. Generally this assistance is related to various programmes of non Plan expenditure. The assistance under this category is given mainly by the Union Finance Ministry and in some cases certain conditions are also attached for the utilization of these transfers. The transfers under this category are mainly in the form of grants and these grants are generally made available to the States for the purposes of expansion of administrative services, improvement of salary of university teachers, loans for national scholarship schemes, loans for purchase of fertilizer, grants for central loan fund, police housing, development of border areas, grant/loan for meeting national calamities like famine, draught and floods etc. The aim of

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80. *For details see B.S.Grewal, *Centre State Financial Relations in India*, chapter V, (1975).*
these grants is to help the States financially outside the Plan. An analysis of the Table 4.1 indicates that whereas under the First Plan period (1951-52) such transfers were just 7.3% of the total Central transfer to the States, with the passage of time it had increased considerably as in Sixth Plan period (1980-85), it has gone to 15.3% of the total Central transfer to the States which has become double to the assistance as was available in 1951-52. It indicates that the Union Ministries especially the Union Finance Ministry also plays an important role in the transference of resources to the States.

(B) Finance Commission v. Planning Commission - An Overview

Both the Finance Commission and Planning Commission play a vital role in the transfer of resources from Centre to the States. However, from the working of both these agencies it comes to the light that there exists some tension between both of them on account of their overlapping functions and powers.

The inauguration of the First Five Year Plan in 1951-52 and setting up of Planning Commission brought about

81. See infra at 43.
82. Lalatha Natraj, An Analysis into the Political Aspects of Planning in India, 82 (1986).
a new development in the 'Federal Financial Relations'. The comprehensiveness of Finance Commission had been seriously restricted by the emergence of Planning Commission. The Finance Commission is a statutory body created by the Constitution whereas the Planning Commission is essentially an extra constitutional body created by an order of Central Government. No doubt the Planning Commission is a body existing outside the Constitution yet the study of various Planning Commissions reveals that it exercises much more influence in the field of transference of revenue from Centre to the States as compared to the Finance Commission a statutory body. Moreover the Finance Commission is a temporary body which comes on the scene after every five years and it has been assigned a limited job of devolution of taxes and assigning fiscal need grants whereas the Planning Commission is a permanent body which has been assigned the job to give grants under Article 282 and loans to the States. After the emergence of Planning Commission the role of the Finance Commission comes to be at best that of an agency to review the forecasts of revenue and expenditure submitted by the States and the acceptance of the revenue element of the Plan as indicated by the Planning Commission for determining the quantum of devolution and grants in aid to be made.

83. Supra note 14.
84. Supra note 31 para 80 at 35.
A large chunk of Central assistance to States is distributed in a discretionary manner and a substantial part of this non-statutory assistance is allocated on the recommendations of Planning Commission. Thus Planning Commission rather than Finance Commission plays a key role in the allocation of resources to the States. In this regard the Third Finance Commission had observed that Finance Commissions are to simply undertake an arithmetical exercise of devolution based on amounts of assistance for each State already settled by the Finance Commission. The evident result is that Finance Commission has to function within the lines already drawn by the Planning Commission. In fact the Union State finances, even annual budgeting are controlled by the Planning Commission through its decisions on Union State Plans. Although the statutory grants and devolution of Union taxes and their distribution is outside the purview of Planning Commission, yet the quantum of these taxes and grants is determined by the Planning Commission through its decisions on the size and sources of the Plans. No doubt, the Constitution makers expected the Finance Commission to work as a balancing wheel in the Indian Federation, yet with the emergence of Planning

85. Supra note 62 at 122.
86. Supra note 31.
87. Supra note 1 at 86.
Commission the Finance Commission has come to play a secondary role. It is alleged that though Planning Commission has no constitutional status yet practically it has over-shadowed the Finance Commission. The table below indicates the flow of funds in the shape of total transfer of revenue from Union to the States through Finance Commission, Planning Commission and Union Ministries from 1951 to 1985.

**TABLE 4.1**

Transfer of Resources from Centre to States (1951 to 1985)

<table>
<thead>
<tr>
<th>S.No. Plan period</th>
<th>Percentage Through Discretionary</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Finance Planning Commission</td>
<td>56.8</td>
</tr>
<tr>
<td></td>
<td>Planning Commissions</td>
<td>43.2</td>
</tr>
<tr>
<td>1. Plan 1951-56</td>
<td>31.2  61.5  7.3</td>
<td>100.00</td>
</tr>
<tr>
<td>2. Plan 1956-61</td>
<td>32.0  46.0  22.0</td>
<td>100.00</td>
</tr>
<tr>
<td>3. Plan 1961-66</td>
<td>28.4  48.9  22.7</td>
<td>100.00</td>
</tr>
<tr>
<td>4. Annual Plan</td>
<td>33.3  35.9  30.8</td>
<td>100.00</td>
</tr>
<tr>
<td>1966-69</td>
<td></td>
<td></td>
</tr>
<tr>
<td>5. Fourth Plan</td>
<td>35.9  31.3  32.8</td>
<td>100.00</td>
</tr>
<tr>
<td>1969-74</td>
<td></td>
<td></td>
</tr>
<tr>
<td>6. Fifth Plan</td>
<td>43.5  41.5  15.0</td>
<td>100.00</td>
</tr>
<tr>
<td>1974-79</td>
<td></td>
<td></td>
</tr>
<tr>
<td>7. Sixth Plan</td>
<td>41.3  43.4  15.3</td>
<td>100.00</td>
</tr>
<tr>
<td>1980-85</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>


A study of Table 4.1 indicates that under the First Plan period (1951-56) the transfers through Finance Commission were only 31.2% of the total central transfers whereas the transfer through Planning Commission were 61.5% just double to the transfers as made on the recommendations of the Finance Commission. However, this trend was gradually curbed as under the Fourth Plan period (1969-74) the total transfers through Finance Commission went up to 35.9% and the transfers through Planning Commission came down to 31.3%. This was a healthy trend which was welcomed by all States. This trend was maintained under the Fifth Plan period also as the transfers made through Finance Commission stood at 43.5% and the transfers assigned on the recommendations of Planning Commission were 41.5%. However, under the Sixth Plan period (1980-85) the trend of transferring more resources through statutory body, was again reverted by transferring 41.3% resources through Finance Commission and 43.4% through Planning Commission. Thus from the study of Sixth Plan period it becomes clear that total discretionary transfers directly or indirectly through the Planning Commission and Union Ministries amount to a large proportion i.e. 58.7% of the total transfers which were wholly outside the purview of Finance Commission. The above discussion makes it clear that for a limited period of ten years ranging from 1969 to
1979 the resources transferred through Finance Commission were more as compared to the Planning Commission, but from 1980 onwards the majority of funds flow through non statutory bodies, which is not a healthy sign in 'Federal Financial Relations'.

It has been observed that the relations between both the Finance Commission and Planning Commission is not cordial as they are envy rather than comradeship. The successive Finance Commissions had not been happy with the working of Planning Commission. The First Finance Commission did not make any mention of the Planning Commission since it was too early for it to feel the pinch. However, the Second Finance Commission pointed out that the functions of the two Commissions the Finance Commission and Planning Commission overlap and so long as both these Commissions have to function there appears to be a real need for effectively coordinating their functions. Likewise, the Third Finance Commission pointed out that the duality of functions was creating confusion therefore, it suggested that either the powers of Finance Commission should be enhanced so as to cover total fiscal assistance that is loan or devolution of revenues or to transfer the Planning Commission into Finance Commission at

89. Supra note 30 para 27 at 13.
an appropriate time. Similarly Dr. P.V. Rajamani, the Chairman of Fourth Finance Commission in a supplementary note observed 'I have no comment to make on such a dichotomy of functions. But I think the relative scope and functions of the two Commissions should be clearly defined by amending the Constitution'.

Though the role of Planning Commission is advisory but it has come to play a very significant and important role in the economic development of the country. In fact it 'has eclipsed in an unmistakable way, the role of the Finance Commission'. As massive financial assistance flow through the Planning Commission in the shape of grants or loans for the Plan projects, therefore, the original intention that the Finance Commission will play the role of a wise man, a judge between the conflicting claims of the States on the one hand and the Centre on the other has been completely defeated with the emergence of Planning Commission. Now the Finance Commission simply determines the revenue gap of each State and provides for filling up the gap by a scheme partly by devolution of taxes and partly by grants.

90. Supra note 31 para 22 at 36.
91. Supra note 32 para 12 at 90.
The States are not happy with the working of Planning Commission and they have expressed their apprehensions about the inherent danger of using the grants and loans as a political weapon against them. Moreover the decisions in Planning Commission are also influenced by political considerations. On the other hand States have shown high regards for the Finance Commission and had accepted its recommendations in a Federal spirit. States are insisting for transferring more resources through statutory bodies so that the increasing trend of allocating resources through discretionary grants is curbed; but the Centre looks at the Finance Commission as an institution which upsets the Plan calculations. Thus there is an urgent need for greater cooperation and coordination between both these revenue transferring agencies.

REVIEW

In the scheme of Federal finance it is implied that the financial resources must be so distributed between the Federal and State Governments that each should have the potential of enjoying adequate resources for expenditure

93. Supra note 62 at 122.
94. Ibid.
involved in carrying out the functions assigned to them. Because it is impracticable to make a clear cut allocation of financial resources, therefore certain devices are used for making Federal fiscal adjustments. In India, the constitutional and extra constitutional agencies play a vital role in the transfer of resources from Centre to the States. The framers of our Constitution anticipated that there is likely an imbalance between the resources and functions of the States, therefore, they provided for constitutional machinery for making an adjustment in the fiscal needs and resources with a view to make the scheme of financial relations flexible and adaptable to the varying needs and reviewable periodically by an independent agency named Finance Commission. The Finance Commission was created with an intention to assure the States that the financial resources will not be distributed arbitrarily between the Union and States. A study of the successive Finance Commissions reveals that while their basic approach had been that the prosperity of States must rest on the solid foundations of a reasonably strong Centre, at the same time the Finance Commissions had recognised the


inadequacy of the resources of the States and therefore they had increased the share of the States in the Central financial assistance considerably. However, the principles as followed by the Finance Commissions so far had not satisfied the States fully.

The Planning Commission a non constitutional agency plays a very important role in the allocation of resources, its activities have encompassed both the Union and States. The Commission formulates the Plans, be it annual or Five Year Plans and after formulating the Plans, it attempts to indicate to each State the financial magnitude of the out-lays for the State Plans and the guidelines regarding the formulation of the sectoral proposals. Since the Planning Commission is a creature of Central Government, since it acts fully to subordinate to the wishes of the government both in its composition, functioning and in the last resort in its working, which pinches the States. S.Shivakumar has described the Planning Commission, 'as a limb of the Government of India'. The National Development Council is the highest representative body of Centre and States in the field of Planning. It plays a vital role in the shaping

97. Supra note 79.
98. Supra note 95 at 1954.
of Planning but its working indicates that more influential States appear to have more say in the fiscal shaping of Planning and the allocation of resources. Likewise, the Union Ministries also play an important role in transferring of revenues from Centre to the States as substantial amount flows through these Ministries.

The facts and figures as given above clearly indicate that massive funds from Centre to the States flow through non statutory agencies as compared to statutory agency. The Finance Commission was created with an intention that it would work as a balance wheel in Indian Federal finance but with the emergence of Planning Commission, it has come to play a secondary role as only a fraction of total income of Government of India comes within the purview of Finance Commission and the major portion of Central financial assistance to the States comes through the non statutory agencies. Thus the States demand for transferring more resources through statutory devolution deserves consideration. Moreover, the relations between both Finance Commission and Planning Commission are not cordial and hence there is an urgent need for greater co-operation between both these major revenue transferring agencies.
