CHAPTER I

INTRODUCTION
India is a federal country. In India there are three layers of governments such as Central Government, State Government and Local Government (Rural/Urban Self Government). In accordance with 7th schedule of the Indian Constitution the jurisdiction of different layers of governments is defined and the responsibilities to be performed at different levels have been fixed. The resources of the country are also divided between the Central Government and State Government based on the principle of fiscal needs and fiscal capacity. There is provision for the transfer of resources from the Central Government to State Government in terms of (a) Taxes, (b) Grants-in-aid and, (c) Borrowings of the State Government from Central Government.

There are some taxes which are levied by the Central Government but collected and appropriated by the State Government, for example: stamp duties on financial agreements/services, excise duties on those items containing alcohol and narcotic etc. There are some taxes levied by the Central Government, collected by the Central Government and the entire amount is appropriated by the State Government, for example: taxes on news paper and advertisement there in, taxes on stock markets, taxes on railway passenger fares and frights, estate duty etc. There are some taxes levied by the Central Government, collected by the Central Government and shared with the State Government on the basis of the recommendation of Finance Commission, such as, income tax and excise duties. There are some taxes exclusively under the jurisdiction of the Central Government, taxes levied by the Central Government, collected by the Central Government and entire amount appropriated by the Central
Government, for example: Custom duties, Corporation tax etc. Similarly
the State Government is also entitled to levy taxes, collect taxes and
appropriate the amount entirely which are coming under the
jurisdiction of the State Government exclusively such as commercial
tax, entertainment tax, professional tax, taxes on vehicle etc. Additional
excise duties levied by the Central Government on items such as
tobacco, cotton, leather etc. in lieu of sales tax which was earlier levied
by the State Governments, the amount is transferred to State
Governments.

There are different types of grants sanctioned by the Central
Government to State Government through which also transfer of
resources takes place from the Central Government to States. These are
(a) Plan assistance, (b) Non-plan assistance (gap filling grants), (c)
special grants sanctioned by Finance Commission, (d) Discretionary
grants sanctioned by the Central Government in accordance with
Article 282 of the Indian Constitution, (e) Centrally sponsored scheme,
(f) Central schemes etc. There are also externally aided projects
implemented in State sponsored by international agencies such as
World Bank, UNDP, Asian Development Bank etc. via Central
Government.

In accordance with Article 291(1) of the Indian Constitution the
State Government can borrow from the Central Government. The
Central Government can also stand as a guarantor for any State
Government if the State Government will borrow from other sources
according to Article 291(l) of the Indian Constitution. However in these
cases it is the discretion of the Central Government. State Governments
are also involved in off the budget borrowings such as borrowings from the General Provident Fund (GPF) of government employees, contingent liabilities, that is borrowing by State sponsored public sector undertakings from market guaranteed by the State Government.

Besides the above provisions there are also other sources through which resources are getting transferred from the Central Government to State Government such as, Backward Region Grant Fund (BRGF), MPLAD Fund etc.

There is always conflict in Indian fiscal federalism between the Central Government and State Government and the State Governments allege that Indian fiscal federalism is asymmetrical being inclined towards the Centre neglecting the interest of States. More than 60 percent of the resources are possessed by the Centre but the Central Government is performing 40 percent of the total responsibilities of the country. However the Central Government does not agree to this point and defends itself stating that in actual practice State Governments are handling more than 60 percent of the country’s resources which is possible due to different provisions of fiscal transfer from the Centre to State through Planning Commission, Finance Commission etc. The general discontentment of the Centre is that State Governments are involved in fiscal profligacy and are legitimizing there created deficits based on fresh borrowings following improvident budgeting. Therefore in the post-globalization era fiscal reforms through medium term fiscal reforms programme has already been introduced to facilitate and motivate States to follow financial prudence, public finance accountability and fiscal efficiency. The objective is to enable States for
deficit stability, debt sustainability and to achieve optimum economic
growth. The Central Government is ready to provide all possible
assistance to any State for its overall economic development provided
the State Government is keenly interested for it conforming to
prescribed targets in the context of fiscal reforms programme.
Therefore, transfer of resources from the Centre to State in the post-
globalization era is meant for inter-state equity based on fiscal efforts by
States being facilitated through different types of assistance such as
incentive funds, debt relief schemes, debt restructuring and debt
swapping by States. The State Governments have implemented the
Fiscal Responsibility and Budget Management (FRBM) Act and are
endeavouring towards fiscal efficiency as per the recommendation of
Twelfth Finance Commission at present.

In this context, the objective of the study is to have a comparative
evaluation of resource transfer from the Centre to States for fourteen
major States in India.

It is an empirical study based on theoretical aspects using
relevant secondary data from different sources such as RBI Bulletin on
State finances etc. A cross section and time series analysis is made
through the application of appropriate statistical and econometric
techniques. Different terminologies of government finances have been
properly placed and studied for useful interpretation of different
parameters estimated, linking with economic theory. The study is a
blending of empirical facts with theoretical base converging towards
solution of emerging problems of State finances in India and its
prospects taking Centre-State financial relations in the framework of Indian fiscal federalism. The dissertation comprises six chapters.

Chapter-I introduces the topic.

Chapter-II analyses exhaustively recommendations of different Finance Commissions.

Chapter-III covers an empirical comparative study of the composition and trend of the resource transfer from Centre to States taking into account fourteen major States in India.

Chapter-IV examines the impact of Central transfer (tax devolution and grants-in-aid) on State economy making a comparative study of fourteen major States.

Chapter-V analyses resource transfer from the Centre to States based on fiscal reforms programme covering a comparative study of fourteen major States.

Chapter-VI is the summary and conclusion of the entire study with the systematic presentation of conclusions of different chapters.