Chapter - 6

ROLE AND RECOMMENDATION OF FINANCE COMMISSIONS AND PLANNING COMMITTEES

Planning based on a clear idea of the magnitude of available resources and anchored, to the extent possible, in self-generated resources is the sine qua non of responsible planning.

In order that the financial position of urban local bodies is reviewed periodically, a state finance commission shall be constituted by the Governor of the State within one year from the commencement of the constitution of India (74th Amendment) Act, and thereafter, at the expiration of every five years. This finance commission will make recommendations to the Governor.

The most Crucial problems in a federation is that of balancing powers and resources between the governments. But in order to correct the imbalances of resources it is worthwhile to have definite provisions and providing a mechanism for their periodical review rather than trust to their being changed when they are proved grossly inadequate and out of date. Despite the detailed and elaborate constitutional provisions for the division of financial resources between the union and the states, the states face the problem of chronic gap between their own resources and the expenditure pattern. That is why our constitution makers were quite cautious on the count and provided for a finance commission under Article 280, to
recommend mainly the financial transfers from the union to the states with a view to reduce vertical as well as horizontal federal fiscal imbalances.¹ But the problems of distributing resources between the states and local Bodies was non-existent because at the time of framing constitution their makers recognized only union and states as two different level of Governments.

The recommendations of the finance commission will cover the following:

- distribution between the state government and Municipalities of the net proceeds of the taxes, duties, tolls and fee leviable by the state,
- allocation of share of such proceeds between the Municipalities at all levels in a state.
- determination of taxes, duties, tolls and fees to be assigned or appropriated by the Municipalities,
- grant-in-aid to Municipalities from the consolidated fund of the state,
- measures needed to improve the financial position of the Municipalities.

The Governor would be free to refer any other matter to the finance commission as he may deem fit in the interest of sound

¹ Article 280 provides for the Constitution of Union Finance Commission to make recommendation for allocation of resources between the states and the centre.
financial management of the urban local government. The finance commission shall determine its procedure and it shall have such powers as are necessary for it to perform its function and which the state legislature may by law, confer on it. In other words, the commission will be free to determine its own, Procedure within the frame-work of powers as may be provided in the state law. It will be mandatory for the Governor to lay before the state legislature every recommendation made by the finance commission together with the Explanatory Memorandum on the action taken in such recommendations.

In compliance with this constitutional stipulation, all the states had setup their state finance commissions. Most of the state finance commissions have submitted their reports to the concerned state governments. Some of them are yet to examine and accept them. It has been made mandatory that the central finance commission shall, inter-alia make specific recommendations with regard to measures that are needed to augment the resources of a state with a view to supplementing the resources of the urban local government in the state on the basis of the recommendations made by the state finance commission. This would provide a proper linkage between the finances of the local bodies, the state governments and the central government.
After independence efforts were made by various committees and commissions in providing more and more financial and functional powers to the local government institution but nothing concrete was actually done till 1992. The constitution (73rd) Amendment Act, 1992 on Panchayat and the constitution (74th) Amendment Act, 1992 on Municipalities are a milestone development in the history of independent India. In fact, these two constitutional amendments aim at transforming the panchayats and Municipalities into strong and viable unit of "self government" and bringing them into the mainstream of the country's social economic development.

An important aspect of amendments in the constitution pertains to the finances of Panchayati Raj institutions and municipal bodies. In fact, strengthening of finance is an essential ingredient of municipal bodies to become viable units of local self-government. With a view to strengthen the financial position of the local bodies, there has been a long standing demand for constitution of state level finance commission. The constitution 74th Amendment Act, 1992 have clearly provided for setting up of state finance commission in each state. To meet the constitutional requirements under the 74th constitutional Amendment, all the states have set up the finance commission at state level.

2 Article 243(l) provides for state finance commission for panchayats and Article 243 Y provides for state finance commission for municipalities.

3 Punjab State has enacted, The Punjab State Finance Commission for Panchayats and Municipalities Act, 1994 for setting up a common. commission for Panchayats and Municipalities.
In this regard, it is very pertinent to have a glance at the actual constitutional provisions with regard to the setting up of the state finance commission. The relevant Article is Article 243-Y with regard to the urban local government.

(A) CONSTITUTION OF FINANCE COMMISSION TO REVIEW FINANCIAL POSITION

Article 243-Y of constitution of India speaks as such:

1. The Governor of a state shall, as soon as may be with in one year from the commencement of the constitution (74th Amendment) Act, 1992 and thereafter at the expiration of every fifth year, constitute a finance commission to review the financial position of the Municipalities and to make recommendations to the Governor as to:

(a) the principles which should govern:

(i) the distribution between the state and the Municipalities 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 Municipalities at 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 Municipalities,
(iii) the grant-in-aid to the Municipalities from the consolidated fund of the state.

(b) the measures needed to improve the financial position of the Municipalities,

(c) any other matter referred to the finance commission by the governor in the interests of sound finance of the Municipalities.

2. The legislature of a state may by law, provide for the composition of the commission, the qualification which shall be requisite for appointment as members thereof and the manner in which they shall be selected.

3. The commission shall determine their procedure and shall have such powers in the performance of their functions as the legislature of the state may, by law, confer on them.

4. The Governor shall cause every recommendation made by the commission under this article together with an explanatory memorandum as to the action taken thereon to be laid before the legislature of the state.

(B) THE PUNJAB STATE FINANCE COMMISSION FOR MUNICIPALITIES ACT, 1994

Punjab was perhaps, the first state in the country which had moved fast once the 73rd and 74th constitutional amendments became effective. It passed the Punjab Finance Commission for Municipalities Act, 1954 on April 19, 1954. The finance commission was constituted on April 22, 1994 with Mr. J.P. Gupta, a retired IAS officer as its
chairman. The commission submitted its report to the Punjab Governor on December 31, 1995. Thus Punjab became the first state in the country to have received the commissions report. In fact the Act requires that the Governor of Punjab should appoint the state finance commission within one year of the commencement of constitution 73rd and 74th Amendment Act, 1992 and thereafter at the expiration of every five years. Accordingly as indicated above, the first State Finance Commission for Panchayats and Municipalities came into existence on 25th July 1994. The Act provides for a chairman and four other members with their term, condition and emoluments for the office. It also specifies broadly the terms of reference, of the finance commission and its functions.

It is submitted that the system would provide for a regular assessment of the financial resources of the Municipalities with reference to the increasing responsibilities thrust upon them by the pace of urbanisation and the growth in the urban economy. It would also put the devolution of resources from the states to their urban local bodies on a rational and stable footing.

(C) FUNCTIONS OF FINANCE COMMISSION

In terms of the constitutional provisions, the Punjab Finance Commission for Municipalities Act, 1994 envisages the setting up of

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5 Section-7, & Section-8, Ibid.
6 Section-9, Ibid.
state finance commission to review the financial position of Local urban bodies and to make recommendations to the Governor as such:

(a) PRINCIPLES OF ALLOCATION OF REVENUE AND GRANTS

(i) Distribution of Taxes: The state finance commission shall make recommendations as to the distribution between the state and the Municipalities 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 urban local bodies such as corporations, municipal committees and notified area committees at all levels of their respective share of such proceeds,

(ii) Determination of Taxes: The state finance commission shall also make recommendations as to the determination of the taxes, duties, tolls and fees which may be assigned to or appropriated by the urban local bodies and

(iii) Grants-In-Aid: The state finance commission shall also make recommendations regarding the grants-in-aid to the urban local bodies from the consolidated fund of the state.

(b) MEASURES FOR IMPROVING FINANCES

To make recommendations as to the measures needed to improve the financial position of the urban local bodies.

7 Section-9(B), Ibid.
(c) MATTERS REFERRED BY GOVERNOR

Under this head, the commission shall make recommendations with regard to any other matter referred to it by the Governor in the interest of sound finance of urban local bodies.

(d) RECOMMENDATIONS OF FIRST PUNJAB STATE FINANCE COMMISSION

The Punjab Finance Commission which was constituted in April, 1994 submitted its report in December 1995. The commission was required to determine the principles relating to the assignment and sharing of state taxes and the devolution of grants to local bodies and also to suggest measures for improving the financial position. Thus in evolving the principles, the commission kept in view the following objectives:

(i) To provide adequate funds to local bodies,
(ii) To enable the local bodies to maintain the essential services at the desirable level,
(iii) To create financial surplus,
(iv) To correct the horizontal and vertical imbalances amongst the local bodies,
(v) To encourage fiscal responsibility and autonomy.

With a view to achieving the objectives, the commission examined three major issues which are:

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8 Extracted from the recommendation of First Finance Commission as studied from chapter 19 of "Development and Local Administration" by Sahib Singh & Surinder Singh, 2001.
(a) Local Financial Authority and Additional Revenue Efforts,

(b) Devolution of State Revenue and

(c) Grants-in-aid.

(a) Local Financial Authority and Additional Revenue Efforts:
The commission examined the revenue authority of Municipalities and the effort for utilizing their authority. The commission found that both from the point of view of utilization of their existing revenue authority and their effort to augment resources are not satisfactory. The commission recommended that the tax domain of the Municipalities should be clearly identified and its enforcement should be made obligating.

(b) Devolution of State Revenue: Devolution of state revenue to the Municipalities is the fiscal instrumentality for reducing the vertical gap arising out of insufficient revenue sources to meet their functional obligations. The commission has recommended that total land revenue should be assigned with Gram Panchayats from 40 percent at present.

The commission has recommended that 20 percent of the net proceeds of stamp duty, Punjab motor vehicle tax, Electricity duty and entertainment tax and entertainment tax [cinematograph shows]. collected by the states be shared with the Municipalities Institutions.
(c) State Grants to Local Bodies: The commission has observed that there is no well developed systems of grants-in-aid to the local bodies in the state. The commission is of the view that the system giving grants should be equitable. It should take into account the fiscal needs as well as the fiscal capacity of the recipient local bodies. The commission is against multiplicity of grants. Three types of grants have been recommended:

(a) General purpose grants
(b) Specific purpose grants and
(c) Per capita grants - per capita grants should be given to weak municipalities to bring them to a level of the average per capita income of the size class to which they belong.

The commission further observes that the financial condition of the local bodies is far from satisfaction as the actual funds available to these institutions are far below to what are necessary to discharge even the obligatory functions of these bodies.

"It is essential that for their growth and stability, the Municipalities should have graving resources in their domain. Apart from the tax, non tax revenues and the transfer from higher levels of Government, the Municipalities should also reply on the institutional loan to promote the development and revenue yielding projects." The commission looked into the need for financial discipline which means economy in expenditure and optimization of revenue effort.
MAJOR PROBLEMS EXAMINED BY THE COMMISSION

The commission, in its analysis of finances of municipalities, in particular, examined the major problems arising from:

(i) imbalance between revenue and expenditure,
(ii) imbalance amongst similarly placed classes of the municipalities,
(iii) dependence of Municipalities on higher levels of the Government and
(iv) inadequacy of tax base and inadequate resource mobilization by the Municipal committees.

BROAD OBJECTIVE FOR MAKING RECOMMENDATION

While formulating its recommendations, the commission also broadly kept the objectives given ahead in view:

- To identify the financial resources for the local bodies that would enable them to perform their functions efficiently and equitably.
- To suggest suitable income to the local bodies to meet their growing mandatory requirements.
- To give weightage to the financially weaker local bodies, while determining their share in the grants-in-aid.
- To ensure a system of equity and efficiency in allocating taxes amongst the local bodies along with incentives.
- The existing schemes, funds, functionaries and structure of departments.
• Measures relating to the performance of local bodies in the matters pertaining to revenue collection, tax administration, expenditure control, efficiency in raising resources, planning and other corrective measures.

• To find ways of ensuring that the expenditure on staff and the administration of the local bodies is in relation to their assigned responsibilities.

• The scope and methods of privatizing the essential services and the functions which have been a drain on the finance of the local bodies.

• The scope of user charges for those services where the beneficiaries can be easily identified.

• The future policy of urban development vis-a-vis the capital cost of the essential services.

• The procedure of levying tax, streamlining of the tax system, the scope and possibility of new taxes and assignment of inelastic taxes such as land revenue, etc.

The commission made an in depth study of several issues and made recommendations some of the important recommendations are as under:

(i) User charges for urban services

(ii) Property tax

(iii) Transfer of Additional excise duty on liquor.
(iv) Grants recommended by the tenth finance commission

(v) Taxation of central Government properties

(vi) Water supply and sewerage

(vii) Privatization

(i) User Charges For Urban Services: User charges are the charges levied for the use or for having access to a given service. The commission noted that the principles of user charges are not being properly enforced by the municipalities for providing civic services. As a result, most of the civic services which should be covered by the principles of user charges are heavily subsidized or given free. It has been found that municipalities do not recover even 1/3rd of the cost of maintenance of water supply and sewerage not to mention the recovery of capital cost. The commission observes that once the user knows that he has to pay for the services which he is availing of, it will automatically act as a curb on excess demand and the services will also not be used excessively and wastefully. Municipalities, which are reluctant to adopt the principle of user charges for reasons of populism, must ensure to shun the habit of dependence on state funds and should more effectively, use user charges in respect of municipal services.

(ii) Property Tax: The poor administration of tax and failure of the municipalities to make proper assessment and recovery of dues, had led to considerable stagnation in the growth of this tax. Exemptions
granted by state government, the shortcomings and poor administration of the rent based system, have resulted in anomalies. The weakness of the present system has, in fact, resulted in a situation where more affluent sections and no residential sector, with a larger capacity to pay, are paying much less while the poorer sections of the populations are subsidizing the richer affluent sections.

The commission has considered the problem and observed that the property tax holds the key to make local taxes more productive and future buoyancy in municipal taxes, seems to lie in strengthening property tax, so that a variety of service taxes should be mounted on it. The commission felt that the evaluation of property tax should be de-linked from the rental value of a property to increase yield and reduce litigation, special surcharge @ 50 to 100 percent should be levied on land or buildings used for industrial or other non-residential proposes and spreading industrial pollution, vacant lands on which no building is erected, as also lands which are being used temporary [for marriage parties, entertainment purposes etc] should be heavily taxed, exemptions from property tax should be drastically reduced, the efficiency of tax correction needs improvement, for greater transparency, all records relating to assessment should be available to any other number of the public on payment of fees, or hearing objections, Municipal valuation commission should be constituted,
filing of statements should be made obligatory and any failure to file such returns or giving incorrect particulars, with a view to evading the tax, should be made punishable under the law.

(iii) Transfer of Additional Excise Duty on Liquor: As noted earlier, Additional excise duty @ 7 percent of the auction money of country liquor and 16 percent of IMFL is collected by the state government in lieu of octroi on import of liquor into limits of municipalities. In order to augment resources of the Municipalities, the commission recommended that this should be enhanced by 10 percent on country liquor and 20 percent on IMFL (Indian Made Foreign Liquor).

(iv) Grants—Recommended By the Tenth Central Finance Commission: The fund as recommended by the 10th finance commission would flow through the state government from 1996 to 97. The funds would be over and above the amounts already being given to the local bodies by the state government. The central finance commission has specified that the funds would not be utilized on salaries and wages. The municipalities would be required to provide suitable matching grant against the funds given to them on this account.

(v) Taxation on Central Government Properties: In the light of recommendations of the local finance enquiry committee (Government of India), it was decided by the central government that payment
should be made to local bodies for service charges in respect of central
government properties. The commission has recommended that steps
to tap this source of revenue should be seriously taken.

(vi) Water-Supply and Sewerages: These two are the premier civic
services provided by the Municipalities as part of their obligatory
functions, the quality and efficiency of these services in a town is an
important indicator of the functioning of a municipality. In the matter
of water management, the performance of the municipalities was
found to be less than the desired level with the following
shortcomings, too much of wastage of water, unsatisfactory billing
and collection, large scale evasion, too much of expenditure, no
system of periodical revision of rates for water supply and sewerage,
large number of connections are not accounted for.

The commission has reviewed the prevailing situation and has
expressed the opinion that the current water rates are adequate for
recovering the maintenance of water supply. It recommended that:

(a) If the Municipal Councils are unable to meet the capital cost of
water supply and sewerage, it should be met by the state
government through purpose grants,

(b) the Municipal will have to improve water management and
billing system to recover the expenditure on maintenance,

(c) the system of sanctioning stand posts, should be abolished,
unless water bills are paid by the community/consumer
collectively.
(d) the water supply rates should be linked with the revision of power tariff.

(e) sewerage charges should be made equal to water rates.

(f) the Municipalities must maintain separate budget and accounts for water supply and sewerage and regular reviews should be held to detect waste full expenditure or shortfalls in revenue.

(g) to provide for cross subsidization for the weaker sections, differential rates should be charged for residential and non-residential buildings. The commercial and industrial connections should be charged at a higher rate. Similarly, lower rates may be charged for low consumption slabs and higher rates for higher slabs.

(h) The entire water supply should be metered, as the present system of flat rates has been an encouragement for wasteful use of water.

(i) running of water supply and maintenance of distribution system, billing and collection of revenue should be progressively privatized.

(vii) Privatisation: The commission has observed that in view of the rapid urbanization and the deteriorating scene in the cities, there is a need to enhance the revenue and reduce the expenditure/costs by the local bodies. In this context local governments can consider the involvement of private sector in the provision of urban services because most of the Municipal services are amendable to
privatization. There is a compulsive need to privatize in the context of the growing demand for urban services. Given the liability of Municipal Government to raise the necessary resources, there is a case to promote to private capital maintain and to augment the civic services in the urban areas. The advantages of privatization, as perceived by the commissions, are:

(a) Cost Reduction (to the extent of 15 to 50 percent)
(b) Increased Coverage
(c) Increased Revenue
(d) Capital Infusion
(e) User Response (Private sector is more responsive)
(f) Increased Efficiency.

The commission was of the view that contracting out is the most common means of involving the private sector. However, privatizing of tax collection is not favored among the people. This is a public function and should be performed by the public agencies only. In the light of this background this commission recommends that load of civic services should be transferred progressively to the private sector so that the people have access to desired level of services on payment basis.

(e) RECOMMENDATIONS OF CENTRAL FINANCE COMMISSION

(i) FIRST FINANCE COMMISSION: The Commission constituted by an order dated 22nd November 1951 list of Recommendation

9 www.financecommissionindia.com
of the commission under Article 270 – 273 of the constitution as follows:-

1. Under Article 270 of the constitution:-
   a) the percentage of the net proceeds in any financial year of the
taxes on income, other than agricultural income, except in so
far as these proceeds represent proceeds attributable to the
constitution or to taxes payable in respect of Union
emoluments, to be assigned to the states, should be fifty five,
b) the percentage of net proceeds of taxes on income which shall
be deemed to represent proceeds attributable to states specified
in part C of the first schedule to the constitution should be
2.75,
c) the percentage share of the net proceeds of taxes on income
assigned to the states should be distributed among the states.

2. Under Article 272 of the Constitution forty percent of the net
proceeds of the Union Duties of excise on tobacco (including
cigars, cigarettes, etc.) matches and vegetable products should
be distributed among the states in part A and part B of the first
schedule except the state of Jammu & Kashmir in proportion to
their population.

3. Under Article 273 of the constitution as grant – in aid of the
revenues each year of the states of Assam, Bihar, Orissa and
west Bengal in the lieu of assignment of any share of the export
duty on jute and jute products.
(ii) SECOND FINANCE COMMISSION:- The recommendation of second Finance Commission in their report dated 30th September, 1957 are as:-

1. The Recommendation under Article 270 (Income Tax), Article 273 (Excise on tobacco), Article 275 (i) grant in aid of the constitution fall in the first category and the necessary orders will be submitted to the President for approval.

2. The Recommendation relating to the distribution of certain union duties of excise the union and the states, the distribution among the states Under Article 269 (2) of the constitution of Estate Duty, property other than agricultural land and tax on, railway fares and the levy and distribution of additional duties in excise in replacement of sales taxes on certain commodities fall in the second category.

3. The recommendations regarding loans have to be implemented through executive orders and necessary action will be taken in consultation with the state Governments.

(iii) THIRD FINANCE COMMISSION:- The recommendations of the third finance commission in its report dated 14th December, 1961 is being laid on the table of parliament. All the unanimous recommendations have been accepted, the report is not unanimous and there were two recommendations on which there was a minute of dissent from one member. These were:-
(a) that a special purpose grant be made to certain states for improvement of communication and,

(b) that 75% of the revenue component of the state plans be included in the scheme of devolution recommended by commission

(iv) FOURTH FINANCE COMMISSION:- The recommendations of fourth finance commission in its report dated 12th August, 1965, that under Article 270 (Income Tax) and Article 275 (i) (grant-in-aid) are two main Articles affected recommendations of Fourth Finance Commission.

(a) The commission has excluded from its assessment of revenue expenditure certain increase in pay scales and dearness allowances increases relating to the state Government employees and employees of local bodies and School teachers effected by the State government of Andhra Pradesh, Mysore and Uttar Pradesh.

(b) The commission’s recommendations were that effect of these liabilities might and be taken into account in fixing the Article 275 grants to be included in the order of the President. These recommendations have been accepted.

(v) FIFTH FINANCE COMMISSION:- The recommendations of the fifth finance commission in its final Report dated 31st July, 1969 relating to the sharing of income tax, union excise duties and
additional duties of excise in lieu of states sales tax and payment of grant-in-aid of the revenues of certain states under Article 275 (1) of the constitution have been accepted. It will be recall that recommendation in repeated tax on Railway fares made in the Commission’s interim report submitted in October, 1968 have already been accepted.

(vi) SIXTH FINANCE COMMISSION:- The recommendations of the sixth finance commission in its report dated 28th October, 1973 relating to sharing of income tax, Union excise duties (including auxiliary duties in the three years 1976 – 77 to 1978 – 79), additional excise duties payment of grants in lieu of the repealed tax on Railway fares and on account of wealth tax on agricultural property were accepted. The commission has recommended the payment of grant – in – aid of the revenue of certain states under Article 275 (i) of the constitution aggregating Rs. 2509.61 crores during the five year period commencing from 1974 – 75 after taking into account the needs of backward states and improvement of standards of essential administration and social service. This recommendation of the commission has been accepted. In computing the grant-in-aid of the order of Rs. 2509.61 crores commission has not taken into account the net interest liability of the states, the account of fresh borrowings and lending during the fifth plan period. The
commission recommended that the net interest liability on this account should be computed and grant—in—aid suitably be modified.

(vii) SEVENTH FINANCE COMMISSION: - The recommendation made by the seventh finance commission in its report submitted to the President on 28th October, 1978 relating to devolution of taxes and duties to the states, grants—in aid under Article 275 of the constitution, financing of the relief expenditure and debt relief to the states.

(a) The Commission’s recommendation, covering a period of five years commencing from the first day of April, 1979, relating to sharing of Income tax, Union excise duties, additional excise duties in lieu of states sales tax, Estate Duty on property other than agricultural land as also payment of grants-in—aid of the repealed tax on Railway fares and on account of wealth tax on agricultural property, have been accepted.

(b) It recommended grant in aid to cover non plan gap on revenue account. Government accepted the recommendation of the commission for payment of Grant— in—aid of the revenues of certain states under the substantive provision of article 275(1)of the constitution, towards meeting their non plan revenue gap, as assessed by the commission, for the five years 1979—84, amounting in all to Rs. 1173.12 Crores.
(c) Commission recommended Grant in aid for up gradation of standards of administration. Government accepted the recommendation for making grant-in-aid to certain states for up-gradation of the standards of administration, equivalent to the revenue and capital provisions which the commission has recommended, subject to the implementation and the monitoring of the up gradation schemes of the manner indicated by the commission.

(viii) EIGHT FINANCE COMMISSION:- The recommendation of the eighth finance commission (November, 1983) are as:

(a) The commission recommended that in respect of the distribution between the Union and State of the next proceeds of Income tax, Union Excises duties, Additional duties of excise in lieu of Sales tax and Estate duty the existing arrangements may continue provisional during the financial year commencing in 1st April, 1984. The commission has recommended that the State of Sikkim may also receive a share of Union Excise duties including excise duties on electricity and Additional excise duties in lieu of sales tax.

(b) Then Commission has also recommend that the existing arrangements with regard to grants made available to states in lieu of tax on Railway Passenger fares and wealth tax on agricultural property may continue provisionally during the year 1984 – 85.
(c) The existing arrangements in regard to financing of relief expenditure by the states affected by natural calamities may also be continued during 1984–85.

(d) The commission has recommended that grant–in-aid under Article 275(1) of the Constitution cover residuary deficits on revenue account may be paid to the states for year 1984–85.

(e) The recovery of small saving loans to state government which was in obeisance during the period 1978-80 to 1983-84 may be deferred during the financial year 1984–85 also.

(ix) NINTH FINANCE COMMISSION:-

(a) The recommendations of the ninth finance commission in its first report 29th July, 1988 regarding devolution of taxes, Union excise duties, Additional duties of Excise in lieu of sales tax, grant–in–aid in lieu of tax on Railway Passenger Fares, Financing of relief expenditure and Debt relief were accepted. In regard to grant–in–aid Government accepted the recommendations of the finance commission relating to revenue component of the state plan may be kept in view by the Planning Commission while finalizing funding arrangements for the annual Plans of the states for 1989–90.

(x) TENTH FINANCE COMMISSION:- The recommendation made by the tenth finance commission in the report submitted to the President on November.26, 1994, that the Report of the Tenth
Finance Commission covering the five years period commencing from April 1st 1995. The commission’s main recommendations related to devolution of taxes and duties to the states, grant–in–aid under Article 275 of the constitution, financing of relief expenditure and debt relief to the states.

Grants to states for financing local bodies:-

The Government accepted the recommendation of the commission for making grants to the states for Panchayati Raj Institutions as well for the Urban Municipal Bodies during the four years period commencing from April 1st, 1996. These grants will be treated as part of the Plan of the state Governments, earmarked to be transferred to local bodies.

(xi) REPORT OF ELEVENTH UNION FINANCE COMMISSION WITH RESPECT TO MUNICIPALITIES: The Eleventh finance commission, which has recently given its report, local bodies has a specific place. In terms of reference it has been mentioned that in case of local bodies:

(a) The commission shall take into account the recommendation of the state finance commission.

(b) Where the state finance commission have not been constituted yet, or have not submitted their reports, the commission will make its own assessment about the manner and extent of augmentation and consolidated fund of the state to supplement
the resources of the Municipalities in the state. While making such assessment the commission -

(i) Shall take into account the provisions required to be made for the emoluments and terminal benefits of the employees of local bodies including those of teachers.

(ii) Shall take into account the existing power of Municipalities to raise financial resources including those by way of raising additional taxes by Municipalities.

(iii) The power, authority and responsibility transferred to Municipalities under Article 243W of the constitution read with schedule eleven and twelve.\textsuperscript{10}

The Eleventh finance commission observed that it was the first time that the Presidential order requires a finance commission to make recommendations in this regard. The commission gave due recognition to Article 243W which envisage that the state legislature may by law endow the local bodies with such powers and functions so as to enable them to function as institution of self-government. The operationalisation of the changes contemplated under the constitution requires action by both the centre and the states. However, the 11\textsuperscript{th} finance commission felt in its report that the pace of empowerment of these bodies to function as institution of self-government has generally been very slow. The finance commission has taken note of

the fact that though the reports of the state finance commission have become available. These focus largely on the pre-devolution position of the Municipalities and don't adequately recognise their emerging role under the 74th Amendment Act.

Accordingly, the Eleventh finance commission recommended that the amount of Rs. 1.600 crore and 400 crore for Municipalities respectively, for each of the five years (2000-2005) and distributed among the states on the following criteria and weights:

1. Population 40 percent
2. Index of Decentralization 20 percent
3. Distance from highest per capita income 20 percent
4. Revenue Effort 10 percent
5. Geographical Area 10 percent

The commission clearly specified that the above grants shall be made available to the respective state, only after the relevant legislative measure are completed for extension of the provisions of 74th Amendment to such areas.

Recommendations of Eleventh Finance Commission:
Recommendation made by the eleventh finance commission in its interim report submitted to the President on January15, 2000 are as:-
Grant to states for financing local bodies: The tenth financial commission had recommended ad-hoc grant to the state Panchayati
Raj Institutions as well for the Urban Municipal bodies. For Panchayati Raj Institutions the tenth finance commission had made an ad-hoc provisional rate of Rs. 100/- per capita for rural population (1971 census) amounting to a total 4,380.93 Crore. For urban local/bodies Rs. 1000 crore has been provided for the year period 1995-2000 on the basis of the inter state ratio of the slum portion derived from the Urban Population figures as per 1971 census. Eleventh finance commission has recommended a 50% increase in the grants to states for local bodies with 80% being earmarked for Rural and 20% for Urban Bodies. Government has accepted the recommendations of the commission.

(xii) RECOMMENDATIONS OF TWELFTH FINANCE COMMISSION

(1) Plan for Restructuring Public Finances:

(a) By 2009-10, the combined tax-GDP ratio of the centre and the states should be increased to 17.6 per cent, primary expenditure to a level of 23 per cent of GDP and capital expenditure to nearly 7 per cent of GDP.

(b) The combined debt-GDP ratio with external debt measured at historical exchange rates should, at a minimum, be brought down to 75 per cent by the end of 2009-10.

(c) The system of on-lending should be brought to an end over time and the long term goal for the centre and states for the debt-GDP ratio should be 28 per cent each.
(d) The fiscal deficit to GDP ratio targets for the centre and the states may be fixed at 3 per cent of GDP each.

(2) Sharing of Union Tax Revenues

(a) The share of the states in the net proceeds of shareable central taxes shall be 30.5 per cent. For this purpose, additional excise duties in lieu of sales tax are treated as a part of the general pool of central taxes. If the tax rental arrangement is terminated and the states are allowed to levy sales tax (or VAT) on these commodities without any prescribed limit, the share of the states in the net proceeds of shareable central taxes shall be reduced to 29.5 per cent.

(b) If any legislation is enacted in respect of service tax after the eighty eighth Constitutional amendment is notified, it must be ensured that the revenue accruing to a state under the legislation should be less than the share that would accrue to it, had the entire service tax proceeds been part of the shareable pool.

(c) The indicative amount of overall transfers to states may be fixed at 38 per cent of the central gross revenue receipt.

(d) The states should be given a share as specified in the following table in the net proceeds of all the shareable Union taxes in each of the five financial years during the period 2005-06 to 2009-10:-
<table>
<thead>
<tr>
<th>State</th>
<th>Share (all shareable taxes excluding service tax) (per cent)</th>
<th>Share of Service Tax (per cent)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>2</td>
<td>3</td>
</tr>
<tr>
<td>Andhra Pradesh</td>
<td>7.356</td>
<td>74.53</td>
</tr>
<tr>
<td>Arunachal Pradesh</td>
<td>0.288</td>
<td>0.292</td>
</tr>
<tr>
<td>Assam</td>
<td>3.235</td>
<td>3.277</td>
</tr>
<tr>
<td>Bihar</td>
<td>11.028</td>
<td>11.173</td>
</tr>
<tr>
<td>Chhattisgarh</td>
<td>2.654</td>
<td>2.689</td>
</tr>
<tr>
<td>Goa</td>
<td>0.259</td>
<td>0.262</td>
</tr>
<tr>
<td>Gujarat</td>
<td>3.569</td>
<td>3.616</td>
</tr>
<tr>
<td>Haryana</td>
<td>1.075</td>
<td>1.089</td>
</tr>
<tr>
<td>Himachal Pradesh</td>
<td>0.522</td>
<td>0.529</td>
</tr>
<tr>
<td>Jammu &amp; Kashmir</td>
<td>1.297</td>
<td>nil</td>
</tr>
<tr>
<td>Jharkhand</td>
<td>3.361</td>
<td>3.405</td>
</tr>
<tr>
<td>Karnataka</td>
<td>4.459</td>
<td>4.518</td>
</tr>
<tr>
<td>Kerala</td>
<td>2.665</td>
<td>2.700</td>
</tr>
<tr>
<td>Madhya Pradesh</td>
<td>6.711</td>
<td>6.799</td>
</tr>
<tr>
<td>Maharashtra</td>
<td>4.997</td>
<td>5.063</td>
</tr>
<tr>
<td>Manipur</td>
<td>0.362</td>
<td>0.367</td>
</tr>
<tr>
<td>Meghalaya</td>
<td>0.371</td>
<td>0.376</td>
</tr>
<tr>
<td>Mizoram</td>
<td>0.239</td>
<td>0.242</td>
</tr>
<tr>
<td>Nagaland</td>
<td>0.263</td>
<td>0.266</td>
</tr>
<tr>
<td>Orissa</td>
<td>5.161</td>
<td>5.229</td>
</tr>
<tr>
<td>Punjab</td>
<td>1.299</td>
<td>1.316</td>
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<tr>
<td>Rajasthan</td>
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<td>5.683</td>
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<td>Sikkim</td>
<td>0.227</td>
<td>0.230</td>
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<td>Tripura</td>
<td>0.428</td>
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<td>Uttar Pradesh</td>
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<td>Uttaranchal</td>
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</tr>
<tr>
<td>West Bengal</td>
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<td>7.150</td>
</tr>
<tr>
<td>All States</td>
<td>100.00</td>
<td>100.00</td>
</tr>
</tbody>
</table>
(3) **Local Bodies**

(a) A total grant of Rs. 20,000 crore for the Panchayati Raj institutions and Rs. 5000 crore for the urban local bodies may be given to the state for the period 2005-10 with *inter-se* distribution as indicated.

(b) The PRIs should be encouraged to take over the assets relating to water supply and sanitation and utilize the grants for repairs/rejuvenation as also the O&M costs. The PRIs should, however, recover at least 50 percent of the recurring costs in the form of user charges.

(c) At least 50 percent of the grants provided to each state for the urban local bodies should be earmarked for the scheme of solid waste management through public-private partnership. The municipalities should concentrate on collection, segregation and transportation of solid waste. The cost of these activities, whether carried out in house or out sourced, could be met from the grants.

(d) Besides expenditure on the O&M costs of water supply and sanitation in rural areas and on the schemes of solid waste management in urban areas, PRIs and ULBs should, out of the grants allocated, give high priority to expenditure on creation of data base maintenance of accounts through the use of modern technology and management systems, wherever possible, some
of the modern methods like GIS (Geographic Information Systems) for mapping of properties in urban area and computerization for switching over to a modern system of financial management would go a long way in creating strong local governments, fulfilling the spirit of the 73rd and 74th Constitutional amendments.

(e) The states may assess the requirement of each local body on the basis of the principles stated by us and earmark funds accordingly out of the total allocation recommended by us.

(f) Grants have not been recommended separately for the normal and the excluded areas under the fifth and sixth schedule of the Constitution. The states having such areas may distribute the grants recommended by us to all local bodies, including those in the excluded areas, in a fair and just manner.

(g) The central government should not impose any condition other than those prescribed by us, for release or utilization of these grants, which are largely in the nature of a correction of vertical imbalance between the centre and the states.

(h) State governments should not take more than 15 days in transferring the grants to local bodies after these are released by the central government. The centre should take a serious view of any undue delay on the part of the state.
(4) Monitoring Mechanism

(a) Every state should set up a high level monitoring committee headed by the Chief Secretary with the Finance Secretary and the Secretaries / heads of departments as members for monitoring proper utilization of finance commission grants.

(b) The monitoring committee should meet at least once in every quarter to review the utilization of the grants and to issue directions for mid-course correction, if considered necessary.

(c) The monitoring committee should be responsible for monitoring both financial and physical targets and for ensuring adherence to the specific conditionality in respect of each grant, whoever applicable.

(d) In the beginning of the year, the monitoring committee should approve finance commission assisted projects to be undertaken in each sector.  

PLANNING COMMITTEES

A striking feature of the new provisions inserted in the constitution by the 74th Amendment Act, 1992 is that they provide for setting up of planning committees at the district/metropolitan level to consolidate the plans prepared by the Municipalities in the district and to prepare a draft development plan for the district as a whole. As the district is a political sub-division of a state which constitute the

11 www.financecommissionindia.com
urban areas, the constitution envisages the district/metropolitan to be the coordinating agencies to ensure that the development plans are successfully performed and completed.

Part IX-A of the constitution contains this novel provision which provides for setting up of a district planning committee to prepare and executive plans for the district as whole. Apart from this, it also provides for the constitution of a planning committee in every metropolitan.¹²

(1) District Planning Committee¹³

Planning and allocation of resources at the district level for the Panchayati Raj institutions are normally to be done by the Zila Parishad. With regard to urban areas, Municipal bodies discharge these functions within their respective jurisdiction. However, some important questions may arise, which would concern the urban rural interface and it may be necessary to take an overall view with regard to development of the district as a whole and decide and allocation of investments between the rural and urban institution.

In order to impart a democratic character to such committee, it is laid down that not less than four-fifth of the total number of members of these committees should be elected from amongst the members of the Panchayats at the district level and of the

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¹² Article 243 ZD provides for District Planning Committee and Article 243ZE provides for Metropolitan Planning Committee.
¹³ Article 243 ZD.
Municipalities in the district in proportion to the ratio between the rural and urban population in the district.

Other details relating to the composition of the said committee, the manner of filling up the seats therein, functions relating to district planning to be assigned to such committees shall be chosen, has been left to the state legislature to decide keeping in view the local conditions.

As per the constitution, there shall be constitution in every state at the district level a district planning committee to consolidate the plans prepared by the Panchayats and the Municipalities in the district and to prepare a draft development plan for the district as a whole.\(^{14}\) The chairperson of every district planning committee shall forward, the development plan as prepared above, as recommended by such committee, to government of the state.\(^{15}\)

Every District Planning Committee as Envisaged Above, Shall in Preparing the Draft Development Plan, Have Regard To:\(^{16}\)

(i) Matters of common interest between the Panchayats and the Municipalities including spatial planning, sharing of water and other physical and natural resources, the integrated development of infrastructure and environmental conservation,

(ii) the extent and type of available resources whether financial or otherwise,

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14 Article 243 ZD (1).
15 Article 243 ZD (4).
16 Article 243 ZD (3).
Role of State Legislature in District Planning Committee:

The provisions regarding constitution of district planning committee are in the nature of basic provisions which are to be supplemented by the laws made by the respective state legislatures, which will define the details as the powers and functions of the planning committees. However, the constitution mandates that the legislature of a state may by law, while constituting a district planning committee make provision with respect to:

(a) the composition of the district planning committees
(b) the manner in which the seats in such committees shall be filled. However, the state legislature shall ensure that not less than four-fifth of the total number of members of such committee shall be elected by, and from amongst, the elected members of the Panchayat at the district level and of the Municipalities in the district in proportion to the ratio between the population of the rural area, and of the urban areas in the district,
(c) the functions relating to district planning which may be assigned to such committees,
(d) the manner in which the chairpersons of such committees shall be chosen.17

17 Article 243 ZD (2).
METROPOLITAN PLANNING COMMITTEE

There are 23 metropolitan agglomerations in the country. Where the metropolitan area would encompass not only the main city corporation but also a number of other local bodies both urban and rural, surrounding the main city corporation. By the end of the century, the number of such metropolitan areas would be about 45. In order to ensure orderly development of the urbanising fringe areas, a proper development plan of the surrounding towns and villages needs to be drawn up in association with the plan of the main city. Further in such areas, there is generally, a considerable amount of investment made by central and state agencies through various development schemes. These need to be coordinated with needs of the metropolitan areas.

With a view to imparting a democratic character to the aforesaid committees, it is laid down that not less than two-thirds of the members of such committees should be elected by and from amongst the elected members of the Municipalities and chairpersons of the Panchayats in the Metropolitan area, in proportion to the ratio between the population of the Municipalities and the Panchayats in that area.\(^\text{19}\)

In view of the constitution, there shall be constituted in every metropolitan area, a metropolitan planning committee to prepare a

\(^{18}\) Article 243 ZF.

\(^{19}\) "Data Base on Municipal Governance in Some Major State All India Institute of Local Self-Governance, Oct. 2002"
draft development plan for the metropolitan area as a whole.\textsuperscript{20} The chairperson of every metropolitan planning committee shall forward the development plan, as recommended by such committee, to the government of the state.\textsuperscript{21}

Every metropolitan planning committee shall, in preparing the draft development plan have regard to:

(i) the plans prepared by the Municipalities and the panchayats in the metropolitan area,

(ii) matters of common interest between the Municipalities and the Panchayats, including coordinate spatial planning of the area, sharing of water and other physical and natural resources, the integrated development of infrastructure and environmental conservation,

(iii) the overall objectives and priorities set by the Government of India and the Government of the State.

(iv) the extent and nature of investments likely to be made in the metropolitan area by agencies of the Government of India and of the Government of the State and other available resources whether financial and otherwise,

(v) consultation carried with such institution and organizations as the Governor may, by order, specify.\textsuperscript{22}

\begin{itemize}
\item \textsuperscript{20} Article 243 ZE (1).
\item \textsuperscript{21} Article 243 ZE (4).
\item \textsuperscript{22} Article 243 ZE (3).
\end{itemize}
Role of State Legislature in Metropolitan Planning Committee:

As said earlier, these provisions regarding constitution of planning committees are in the nature of basic provisions which are to be supplemented by the law made by the respective state legislatures, which will define the details as the powers and functions of the planning committee. However, legislature of a state may, by law, while constituting a metropolitan planning committee makes provision with respect to:

(a) the composition of the metropolitan committees,

(b) the manner in which the seats in such committees shall be filled. However, not less than two-thirds of the members of such committee shall be elected by and from amongst, the elected members of the Municipalities and the chairpersons of the panchayats in the metropolitan area in proportion to the ratio between the population of the Municipalities and of the Panchayats in that area, the representation in such committees of the Government of India and the Government of the State and of such organizations and institutions as may be deemed necessary for carrying out the functions assigned to such committees,

(c) the functions relating to planning and coordination for the metropolitan area which may be assigned to such committees,

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23 Article 243 ZE (3).
(d) the manner in which the chairpersons of such committees shall be chosen.

In view of the constitutional requirements, the numbers of state legislatures have adopted the above provisions in their respective statues. Section 42-B in the Punjab Municipal corporation Act, 1976 has made clear cut provision for the setting up of a District Planning Committee to consolidate the plans prepared by the panchayats and the Municipalities in the district and to prepare a draft development plan for the district as a whole. Similarly, section 42-C in the Punjab Municipal Corporation Act, 1976 provides for the setting up of a Metropolitan Planning Committee for the overall growth and development at the metropolitan level.

Thus, the setting up of a District Planning Committee at the district level and a Metropolitan Planning Committee of the Metropolitan level are some of the novel provisions under new system of Panchayati Raj and Municipalities introduced in the constitution by the 73rd and 74th Amendment Act, 1992.