CHAPTER VI

SUMMARY AND CONCLUSIONS
It is said that finance is not mere arithmetic but finance is a great policy. Finance is not only the bed-rock of any modern federation but the financial policy of a federation has a tremendous impact on the lives of the citizens and on their levels of living. A federation will stand or fall by the adequacy or otherwise of its economic constitution. So, financial provisions of a federation and the intergovernmental relations constitute the most important aspect of a modern federation. An analysis of the division of taxing and spending functions among different levels of government and the way the financial provisions are worked out in actual practice should naturally be of interest. The financial relations of a newly formed federation like India which is also a developing country need to be studied in depth in comparison with financial relations in well established federations.

The Indian federation with one Union government, twenty-two state governments and nine union territories, completed thirty-six years of its existence. During this period, Centre-State financial relations have assumed enormous importance. At the aggregate level the total of taxes and grants transferred to the States increased to Rs. 14,003 crores in 1983-84 as against
the average annual transfer of Rs. 286 crores during the first plan period. In addition, loans advanced by the Centre to the States amounted to Rs. 4903 crores in 1983-84. In spite of this transfer of resources from the Centre to the States there does not appear to be alround satisfaction. Individual states complain about the resources transfers—as too little, delayed and discriminative and demand for greater financial autonomy to States. It is said that the States have been reduced to the status of 'beggars' before the Centre. The Finance Minister of Punjab is reported to have stated that all elastic sources of revenue like corporation tax, excise duty were with the Union while inelastic sources like water, passenger tax which caused public resentment, if raised, were with the States. He said that if this practice were to be continued, it would lead to serfdom of the States. The Chief Minister of Karnataka declared that strong states are imperative for a powerful Centre. He identified over centralisation of resources as the prime factor for the poor rate of economic growth in the country. Changes in the political scene of the country with different parties having power in the States and in the Centre remarkably affected the character of federal financial relations in India. Inter alia, a review of Central-State financial relations became so important that the government of India found it necessary to appoint a Commission under the Chairmanship of Justice Sarkaria
to examine the myriad aspects of the Centre-State relations.

In this context, a study of the financial relations of the Union with one of the States, namely Andhra Pradesh, is attempted. Andhra Pradesh is the fifth largest State in the country both in respect of geographical area and populations. According to 1981 census Andhra Pradesh has 7.8 per cent of the population of India and 0.4 per cent of the geographical area. Andhra Pradesh is one of the first few states to be reorganized largely on the basis of language. Andhra Pradesh State came into existence on 1st November 1956. So, the first full financial year after the formation of the State is 1957-58. The financial relations of Andhra Pradesh and the Indian Union have therefore been studied from 1957-58 to 1984-85. The study is primarily based on secondary data. Simple statistical tools have been used for purposes of comparisons. Estimates of elasticity of different taxes in the country have been adopted from the studies of Reserve Bank.

The Andhra Pradesh model in respect of financial relations has been compared with the 'all states model' - 'the notional model' financial model of all the twenty-two states put together. Resources received by Andhra Pradesh from the Centre under the head-shared taxes, grants and loans have been calculated as percentage of the aggregate of such transfers to all the states put together during the period.
The revenue resources of Andhra Pradesh may be classified under the following heads as in the case of all other states under the provisions of the constitution.

1. Exclusively State taxes - land revenue, general sales tax, Motor vehicles tax, State excise duties, entertainment tax etc. Revenue from taxes imposed, collected and retained by the States is described as State's own tax revenue (SOTR).

2. Under Article 270 of the Indian constitution, the Andhra Pradesh government like all other States has a share in the net proceeds of income tax imposed and collected by the Union government.

3. Under Article 272, Union government imposes excise duties and collects them. It is not obligatory for the Union government to share the proceeds of Union excise duties with the States. At the same time, the Centre is not prevented from sharing the proceeds of the Union excise duties with the States. Successive finance Commissions recommended the distribution of Union excise duties to States in varying proportions.

The two categories of tax revenue mentioned above, generally go by the name of 'Shared taxes' in one case the Union government imposes the income tax, collects it and compulsorily distributed it to the States; in another case, though the Union government imposes and collects the Union excise duties their distribution is optional. Nevertheless, States have been
getting a share of the Union excise duties also. In addition, the state governments also get what are called assigned taxes as shown below:

4. Under Article 269 of the constitution, stamp duties are levied by the Union but collected and appropriated by the States.

5. In the case of certain other taxes they are levied and collected by the Union but assigned to the States completely— for example, estate duty, taxes on railway fares and freights inter-state sales tax etc. (Article 269)

In addition to the shared taxes and assigned taxes the government of India may also give such sums of money as determined by the Parliament as grants-in-aid to the States. This is an important provision from the point of view of fiscal federalism. Making use of this Article, regional inequalities can be reduced, the levels of administration in different states can be pushed up. In addition to the statutory grants under Article 275, the Union government may also make grants for the states for any public purpose. Grants under this Article are discretionary (Article 282).

Sharing of taxes and giving of grants are the principal measures of financial adjustment between the Centre and the States. However, the Union government may also make loans to state governments.
The most important provision relating financial adjustment is the provision relating to the appointment of the Finance Commission by the President (under Article 280) in every five years or for such shorter terms that the President thinks necessary. The Finance Commission, after a thorough review of the financial position of the Union and the State governments, recommends the devolution of resources from the Centre to the States. The Finance Commission is thus expected to impart the necessary dynamism and flexibility to the provisions relating to the financial relations. The role of Finance Commission of India is thus different from the role of Commonwealth Grants Commission of Australia. It is a matter of regret that there is no effective body to supervise the financial relations between two Finance Commissions—that is, after the submission of the report of one commission and the appointment of another commission. Though the Planning Commission also advises on the transfer of resources from the Centre to the State its advice is mainly restricted to plan grants. There is, therefore, the need for the institution of an agency of a permanent character to constantly review the Centre-State financial relations.

Between 1950 and 1984, eight Finance Commissions have been appointed in India—the first was in 1951. The eighth Finance Commission submitted its report in April 1984. Succe-
ssive Finance Commissions recommended larger and larger devo-
lution of resources from the Centre to the States. During
1951-52 a sum of ₹70 crores was transferred to the States
under head of taxes and grants. In 1981-82 the corresponding
amount was ₹4566 crores. The total devolution of resources
from the Centre to the States as a percentage of Central revenue
receipts are as follows:

<table>
<thead>
<tr>
<th>Period</th>
<th>Percentage</th>
</tr>
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<tbody>
<tr>
<td>First Plan Period</td>
<td>36.4</td>
</tr>
<tr>
<td>Second Plan Period</td>
<td>31.3</td>
</tr>
<tr>
<td>Third Plan Period</td>
<td>31.3</td>
</tr>
<tr>
<td>Annual Plan Period</td>
<td>31.4</td>
</tr>
<tr>
<td>Fourth Plan Period</td>
<td>36.4</td>
</tr>
<tr>
<td>Fifth Plan Period</td>
<td>30.7</td>
</tr>
<tr>
<td>Sixth Plan period</td>
<td>32.6</td>
</tr>
</tbody>
</table>

The foregoing figures show that the average of aggregate
transfers from the Centre during fifth and sixth plan periods
was only 31.6% which was less than that during the
fourth plan period i.e., 36.4% per cent. This shows that the
aggregate transfer of resources on a percentage basis from the
Centre to the States has been on the decline. An important
factor to be remembered in this context is that the elasticity
of taxes which are shared with the States is generally less
than that of taxes which are shared either to a small extent
optionally or not shared at all with the States. For the period
1960-61 to 1978-79 the elasticity of income tax revenue with
respect to national income was less than unity at 0.8824 whereas the elasticity of corporation tax which is not shared with the states, (for the same period) was 0.9373. That is corporation tax was relatively more elastic than income tax.

As the Union Finance Minister, in his long term fiscal policy statement of December 1985, stated the indirect taxes as a whole have displayed better growth and buoyancy but among them customs have grown faster than excise. As a result, the share of customs in the taxes collected by the centre has gone up. The contribution of excise, though still the largest, has undergone a decline. The buoyancy of excise has suffered because of a variety of factors including numerous exemptions and concessions which have given rise to substantial administrative and legal complexities. It is obvious that the elasticity of customs and corporate taxes is higher than that of income tax or Union excise duties.

While Andhra Pradesh received 8.8 per cent of aggregate of transfers from the centre in 1957-58, the percentage in the subsequent years as follows:

1967-68 ... 7.2.
1977-78 ... 7.9
1982-83 ... 7.10

The figures mentioned above clearly reveal that, the share of Andhra Pradesh in the aggregate of transfers has been
on the decline from 1977-78. Further the relative share of Andhra Pradesh in the aggregate of transfers at 7,10 in 1982-83 was less than its relative share in both total population and geographical area of the country.

As has been already stated, taxes, grants and loans are the principal constituents of the devolution of resources from the centre. Of the three constituents, tax sharing is the most important. After taking into account the transfer of tax resources normally any revenue gap that is left in the budgets of the states, is filled normally through grants. Many advocates of states' autonomy also believe that it is desirable to have a larger percentage of transfers under statutory provisions preferably undertaxes. In the case of Andhra Pradesh the relative share of (shared and assigned) taxes in the total devolution of resources was as follows:

<table>
<thead>
<tr>
<th>Year</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>1957-58</td>
<td>55 per cent</td>
</tr>
<tr>
<td>1967-68</td>
<td>52.51 per cent</td>
</tr>
<tr>
<td>1977-78</td>
<td>50 per cent</td>
</tr>
<tr>
<td>1982-83</td>
<td>54.4 per cent</td>
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</table>

Grants are given by the Union government to the states both under Article 275 and Article 282 of the constitution. Grants given to Andhra Pradesh as a percentage total devolution of resources to Andhra Pradesh has been as follows:

<table>
<thead>
<tr>
<th>Year</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>1957-58</td>
<td>44.9 per cent</td>
</tr>
<tr>
<td>1967-68</td>
<td>47.5 per cent</td>
</tr>
<tr>
<td>1977-78</td>
<td>49.6 per cent</td>
</tr>
</tbody>
</table>
The share of Andhra Pradesh in the shared taxes of all the States in 1960-61 was 8.07 and declined to 7.83 in 1981-82.

Grants-in-aid to Andhra Pradesh in the total grants-in-aid to all States also shows a decreasing trend. It was 7.57 per cent in 1960-61 whereas it was 6.11 per cent in 1981-82.

On the other hand, States' own tax revenue of Andhra Pradesh was above 8.5 per cent of the aggregate own tax revenue of all States put together both in 1960-61 and 1981-82. This shows that the share of Andhra Pradesh in the Central transfer has been on the decline.

As the eighth Finance Commission has rightly observed, there is nothing basically wrong in growth of the public debt. With the expanding public functions no government in a developing economy can undertake large scale programmes of development without resource to borrowing. The relationship between Union and the States in the task of economic development is one of partnership. As such, loans constitute an important mechanism for transfer of resources to the States. The net borrowings of Andhra Pradesh Government from the Union has been on increase year after year. While the net borrowing amounted to Rs.15 crores in 1957-58 its magnitude increased to Rs.206 crores in 1984-85. At the end of 1984-85 the total amount of outstanding loans of Andhra Pradesh was Rs.1099 crores. When a creditor has to help the debtor, the shortest and the simplest way is to reduce the debt liability
either in terms of the principal or in terms of the rate of interest. Write off, of loans or reduction in the rate of interest by appropriate conversions, extension of the period of repayment of the loans have been the principal instruments for reducing the repayment liabilities of the States. Under the recommendations of the eighth Finance Commission Andhra Pradesh Government gets the relief of Rs. 405.20 crores. This constitutes 17.7 percentage of the total relief provided to all states in India.

An associated problem which has manifested itself in Union-State financial relations is that of over-drafts. Unauthorised over drafts are a sign of financial indiscipline in that the concerned state government over spends without any regard to availability of resources. Fortunately the problem of overdraft of Andhra Pradesh to the Centre also has been resolved along with that of the other states with effect from 28th January 1985.

Economic development is a joint venture of all the tiers of governments. In this supreme task, the centre and the states are partners and not rivals. The Union government and the state government should co-operate with each other for the welfare of the Nation.