CHAPTER I

INTRODUCTION

1.1. Introduction

The village Panchayat is the basic local government unit in rural India. Though Panchayats have been in existence for a long period of time, the present system clearly marks off from the past in respect of powers, functions and financial resources. Panchayats have now a major role as instruments of rural reconstruction and development. They have been given wider powers and financial resources not only because they are institutions of political participation but institutions of social and economic development. Sometimes, it becomes the joint responsibility of the centre state and local governments to perform certain important functions. It becomes necessary to combine national conception with local execution for implementing certain programmes. Thus every Panchayat has its contribution not only to the development of the particular area under its jurisdiction but also to the whole nation. There is a growing need of making use of local interest, local knowledge and local participation for the administration of every nation. “There are some functions which can be best performed by local authorities only. Such functions need local attention and adaptation to circumstances. They cannot be standardised on a state or national level”. Hence the consolidation and reorganisation of local bodies have been felt at all times. Scientific consolidation and reorganisation of local bodies calls for not only the provision of more efficient structure for
them but also providing them with sufficient finance to discharge their duties efficiently. The 73rd Constitutional Amendment Act 1992 is a big step forward in this direction. Accordingly more powers and functions have been assigned to Panchayats.

The devolution of functions to Panchayats cannot be considered in isolation of finance required to perform these functions. Increasing functions imply increasing need for resource. The local government should have the freedom of selecting and implementing their own programmes, for which they should have the freedom to raise funds independently. "Upon adequate revenue provision depends the ability of local authorities to discharge any responsibilities; upon some sources of revenue being local, depends the prudence and independence of local authorities; upon predictability of revenue depends their ability to plan for the future; upon the equity of their local tax system, depends much popular support".²

Maddick thus emphasises the importance of local finance in general and revenue generated locally in particular.

1.2. Definition and Nature of Local Finance

Finance in its original meaning denotes the payment of fine. The specialised use of the term as equivalent to the management of public expenditure and receipts came to be used later. Prof. Adam defines finance as
“an investigation of public expenditure and public income and all those varied relations implied in considering such expenditure and income”.

Prof. Plehn defines it as “the science which deals with the activity of the statesmen in obtaining and applying the material means necessary for fulfilling the proper functions of the state”.

According to the above definitions the science of finance deals with the revenues and expenditure of the state. However the subject of finance in the modern times is broadly divided in to two classes - Public finance and Private finance. Public finance deals with the requirements, receipts and disbursements of funds in the case of governmental institutions. Private finance is concerned with the requirements, receipts and disbursements of funds in the case of individuals and non-governmental organisations.

“The complex problems that centre around the revenue expenditure process of government is referred to traditionally as public finance”.

According to Taylor “Public Finance deals with the finance of the public under the institution of the government. The finances of the government include the raising and disbursement of government funds”.

The above definitions point out the nature of public finance as the revenue and expenditure of the governments of any kind.
Local finance is that branch of public finance which deals with the resources that are available to the local bodies to meet their needs of expenditure. A comprehensive study of this subject embraces not merely the sphere of raising resources but of expenditure too. For any sound system of local finance there has to be a clear distribution of functional responsibilities among various echelons of the government as also a well defined division of their financial responsibilities. Thus the finance of local government must correspond to the functions assigned to them.

1.3. Brief History of Local Governments in India

Self governing village communities had existed in India from the earliest times. They are mentioned in the Rigveda which dates from approximately 1200 B.C. "Rigvedic evidence shows that the Aryan society was divided in to Janmans (villages) Visas (blocks) and Janas (several Visas together) - Rigveda II 26.3". In the course of time, these village bodies took the form of Panchayats - an assembly of five persons to look after the affairs of the village. Caste Panchayats were also there to ensure that persons belonging to a particular caste live according to its code of ethics. Village Panchayats had a village assembly whose executive body consisted of representatives of various groups and castes. They continued to have the same characteristics even during the medieval and Mughal periods. Although their judicial powers were curtailed under the Mughals, local affairs were not regulated from above.
The British government replaced the village communities with formally constituted institutions of village administration. "It is a historical fact that local government in India, in the sense of an accountable representative institution was the creation of the British". In 1687, a Municipal Corporation came to be formed in Madras. Established on lines with the British model of a town council, this body was empowered to levy taxes on buildings. Thereafter Municipal Corporations were formed in other major towns. Taxation powers were also widened. However these bodies had only nominated members.

In 1870, the Viceroy Lord Mayo got a resolution passed by his council for the decentralisation of power. It was indeed a land mark in the history of local government under British regime.

Ripon Resolution was considered to be a turning point in the history of local self government in India. The resolution of May 18, 1882 during the Viceroyalty of Lord Ripon, contained provisions for the large majority of elected non-official members in the local boards to be presided over by a non-official chairperson. Then two thirds of the total membership of the local rural boards would be composed of elected representatives. In 1907, the government set up Royal Commission on Decentralisation which submitted its report in 1909. This commission comprised of five Englishmen and only one Indian. The
commission recommended the establishment of village Panchayats with wide powers and functions. But the recommendations remained largely on paper.

The Montagn-Chelmsford Reforms of 1919 made local self government a transferred subject. It meant that local self government was brought under the domain of Indian ministers in the provinces. In various provinces and native states, Acts were passed for the establishment of village Panchayats.

The government of India Act 1935, is another important landmark in the history of Panchayats in India. Legislations were enacted in many provinces for further democratisation of local self government institutions.

1.4. Post - Independence Period

The history of Panchayati Raj in India after independence has been showing a series of ups and downs. The Ashok Mehta Committee divided the journey of Panchayati raj in three phases.

1. The phase of ascendency (1959-'64)
2. The phase of stagnation (1965-'69)
3. The phase of decline (1969 - ')

After the submission of Ashok Mehta Committee Report, many developments took place resulting in the revival, stagnation and ascendency of Panchayat raj.
Mahatma Gandhi's idea of the revival of the 'little republic' has much influence in the development of Panchayats in India. Gandhiji wrote “India's independence must begin at the bottom. Thus every village will be a republic or a Panchayat having full powers. The village Panchayat should constitute an integral part of our constitution, if our independence is to reflect the people's voice. The greater the power to Panchayats, the better for the people”.

Part IV of the Constitution of India contains the provisions of the institution of the Panchayati Raj. Article 40 of the Constitution, one of the directive principles of state policy lays down that “the state shall take steps to organise village Panchayats and endow them with such power and authority as may be necessary to enable them to function as units of self government”.

'Local Government' has also been mentioned in Schedule seven, List II (State List) 5 which reads “Local government that is to say the constitution and powers of municipal corporations, improvement trusts, district boards, mining settlement authorities and other local authorities for the purpose of local self government or village administration” It should be particularly noted that the term 'Panchayat' has not been included here.

Many Commissions and study groups were constituted by the government of India to study the various aspects of local self government in India and to give recommendations to the government.
Rajasthan was the first state in independent India to have the Panchayati raj system. It was inaugurated by the Prime Minister Jawaharlal Nehru on October 2, 1959 at Nagpur. By 1960 all the states had passed Panchayat Acts.

1.5. Constitutional Amendment

In September 1991, the Narasimha Rao Government introduced the 73rd (Panchayats) and 74th (Nagarapalikas) constitutional amendment Bills. They were referred to a joint select committee of parliament. The Lok Sabha passed the bill on 22nd December 1992 while the Rajya Sabha passed it in the following day. The President of India gave his assent on 20th April 1993 and the Act was brought in to force by a government notification on 24th April 1993.

The 73rd Constitutional Amendment has given only general guidelines for the effective functioning of Panchayati Raj Institutions in India. It granted the Panchayati Raj Institutions a constitutional status and uniformity with a three tier system. It makes compulsory the election to the local bodies in every five years, making the Election Commission responsible for the conduct and supervision of elections to local bodies. It also provides for more financial autonomy with the provision to constitute State Finance Commission. All the states, expect those exempted enacted fresh legislation before the dead line of 23rd April 1994. The Act is not applicable to Jammu and Kashmir, Mizoran, Nagaland and certain scheduled areas of the country.
1.6. History of Panchayati Raj in Kerala

The Kerala state came into existence on 1st November 1956 following the reorganization of states on linguistic basis. The territories of the princely states of Travancore and Cochin and the Malabar District of Madras State were merged to form the state.

The first elected government in Kerala constituted a committee under the chairmanship of the then Chief Minister E.M.S. Namboothiripad for administrative reforms. The Committee submitted its report in July 1958 which recommended the strengthening of Panchayats as a basic and viable unit of administration. On the basis of the recommendations of the committee the Kerala Panchayat Bill and later District Council Bills were introduced in the state assembly. But neither of them could be enacted into law as the government was dismissed and the assembly was dissolved. After the new government was formed, the Kerala Panchayat Act 1960, the Kerala Municipalities Act 1960 and the Kerala Municipal Corporation Act 1961 were passed. Accordingly new Panchayats came into existence in January 1964. It was a one-tier Panchayati raj system provided by the Act. In 1964, the government introduced a Kerala Panchayat Union Councils and Zilla Parisads Bill which was in consonance with the recommendations of Balwantrai Mehta Commission. But the Bill was not passed as the government fell within a few months.
The Kerala Panchayati Raj Bill 1967 which provided for a two-tier system of Panchayats introduced in the assembly was also not passed. The Kerala District Administration Bill introduced in 1971 had also the same fate. The Kerala District Administration Bill was again introduced and passed by the legislature in 1979 after some amendments. But the government which came to power immediately after this, stopped to implement the Act. Only in December 1990, the government announced election to the District Councils which took office by February 5, 1991. Thus two-tier system of local government came into existence for the first time in Kerala.

The 73rd Constitutional Amendment Act 1992, made it mandatory the creation of Panchayats at three levels. Fresh legislations were made in the state assembly to comply with the provisions of the 73rd and 74th amendment on 23rd April 1994. Thus the Kerala Panchayat Act 1994 came into force. The Act makes provision for the formation of Gram sabhas ward-wise in each Panchayat. These Gram sabhas have a number of supervisory and monitoring powers related to development activities. They have to assist in the identification of beneficiaries and mobilisation of community efforts. There are at present 991 Grama Panchayats, 152 Block Panchayats and 14 Zilla Panchayats in Kerala.

The first State Finance Commission was constituted by a notification dated 23-04-1994 under clause I of Article 243 of the constitution of India and
section 186 of the Kerala Panchayat Raj Act, 1994, to study the financial position of the Panchayats and to make recommendations to the governor. The commission submitted its interim report on 30th September 1995 and the final report on 29th February 1996. On July 4, 1996 the Kerala Government constituted a committee on decentralization with Dr. Satya Brata Sen as its Chairman. It submitted the interim report in August 1996 and final report in 1997. Regarding the peoples participation, the Sen Committee observed "The corner stone of decentralised democratic governance is peoples participation anywhere in the world and notably in Kerala. Mobilisation and not even consultation is participation. Genuine participation consists of dialogue and partnership leading to full involvement in decision making in the allocation and utilisation of resources meant for collective good that constitutes genuine participation". The committee recommended that there should be provision to have participatory community structure to enable the poor to have a say in the development matters.

1.7. People's Plan Campaign

In 1996, the Kerala State Planning Board resolved to initiate a 'People's Plan Campaign' to empower the Panchayats and municipal bodies to draw up ninth plan schemes within their respective areas of responsibility. The Planning Board expected that 35% to 40% of Kerala's ninth plan would consist of schemes formulated and implemented by local bodies with people's involvement.
"A bane of the planning experience so far in the country has been the tendency towards over centralisation leading to usurpation of societal rights and bureaucratisation of economic life. Planning from below has been posed as an antidote to the above centralisation tendency".11

The People's Plan Campaign initiated in August 1996 is still continuing even after the new government took office. With people's participation, not only at the decision making stage, but at the executing of the projects implemented by the Panchayats as well, it is praised as a model to all other states. It has attracted attention world wide. Franke and Chasin has rightly observed "Kerala's decentralisation programme is probably the largest of its kind in the World".12

1.8. The Problem and its Importance

The development of decentralised administration and the establishment of Panchayati raj institutions call for a detailed study of the finances of Panchayats. This is particularly true because the functions of any government and finance are inter related. Without sound finance, no sound government is possible. Functions cannot be performed without finance and finance without functions has no justification. Henry Maddick opines that there may be very high marginal return in the form of local endeavour and voluntary effort. Even then, they need adequate finance. "Local government is no different from any other form of government, in that absence of income means an almost complete
One of the major problems of local government in India is finance. Although the Panchayats in Kerala have a much better financial situation compared to the rest of the country, they are inadequate to meet the development and maintenance functions assigned to them. After the 73rd Amendment to the Constitution and the Kerala Panchayati Raj Act 1994, the local self-governing institutions in Kerala have been granted the power to plan for the locality. A sizeable part of the state plan, i.e., 35% to 40% under the IXth plan consists of the plan prepared by the three-tier Panchayats. Funds have been released to the Panchayats for the execution of the projects prepared by them under the participatory planning process initiated by the State Planning Board. These developments impose additional burden on the Panchayats to mobilise more resources, allocate them in an optimum manner and ensure accountability. Even though the Panchayats are getting funds from higher governments in the form of grant-in-aid, the importance of own-revenue cannot be ignored. If one goes through the reports of various committees and commissions on local finance, one would generally come across a diagnosis of the existing financial arrangements and subsequently a set of solutions keeping in view the responsibilities assigned to the local bodies for the provision of the service and for the promotion of local level development. All the commissions on local finance stress the importance of improving the finances of the Panchayats by allocating certain permanent and
independent sources of revenue. Panchayats being the primary government unit at the grass root level, can take up the responsibility of collecting taxes from the local people and are answerable to them. The Sen Committee's view is worth mentioning here. "It is necessary to underscore the fact that the growing expenditure responsibilities must not be seen independent of revenue raising responsibilities. The 'You-pay-I-spend' syndrome should not be allowed. The local bodies need to be enabled to raise user charges and fees besides institutional finance".14

However, the taxable capacity of the people which the higher governments left untapped is very low. So local authorities have to depend on higher authorities for the share of taxes collected by such authorities. Moreover all the functions performed by local bodies are not local in all the aspects. The distinction between functions of national importance and those of local importance cannot be made in certain cases. That is why a share of revenue of the higher government should be transferred to local bodies.

Grant-in-aid forms a major item of revenue to local bodies. The Taxation Enquiry Commission, 1953, expressed its opinion in clear terms regarding grants-in-aid. "Normally grants-in-aid should be preferred to assignments of shares of taxes as a method of financing local bodies".15 The main object of grants-in-aid is to enable local authority to meet the expenditure needed for the performance of the functions assigned to it. Gram Panchayats have major roles
in providing certain services, in the development of infrastructure and in augmenting the agricultural and industrial production, all of which are of national importance. Hence the importance of grants-in-aid for the performance of such functions. However it is to be allocated among the Panchayats in a justifiable manner. "The need for a better sense of direction and clear evolution of objective criteria and norms for inter governmental transfer of resources is felt now more than any time in the past". 16

Finance includes expenditure too. The relative importance of local government in a country is really evaluated by the share of its expenditure in the total government expenditure. Panchayats are not only staff agency for development planning but also the line agency, i.e., the implementation agency. It is executing the plan schemes for which plan funds are available from the state government. Along with this it would have to carry out certain duty bound schemes for which non-plan funds from the state government as well as own fund of the Panchayat are available. To this extent it is significant to have a deep study of the management of the expenditure by the Panchayats.

It may be noted that local finance operates in a federal system with many constraints. Over the year, the system we have evolved in our country is one of centralisation of revenues and decentralisation of expenditure. Assigning independent and stable revenue is a surer way of improving the finance of the Panchayati Raj Institutions. If the decentralized planning currently going on
leads to additional resource mobilisation and greater self-reliance, the goals of decentralisation will be realized. It is in this context that an analytical study of local finance assumes importance.

1.9. Review of Literature

The literature on rural local finance can be classified in to empirical works and non-empirical works. The empirical studies include various aspects like resource mobilisation, its utilization, institutional relationship and development, the pattern of rural local revenue, the pattern of rural local expenditure, the trend of rural local expenditure, the trend of local finance revenue and expenditure and the management of local finance.

'Local finance in Perspective' is the title of the study made by K. Venkitaraman. It highlights the problem of local bodies in the management of their finance. It suggests ways to overcome those problems and concludes that the problems of local finance are not capable of easy solutions suggesting a patient study of all relevant data and examination of the problem in its correct perspective.

'Study of the financial resources of Panchayati Raj institutions in Andhra Pradesh, Maharashtra and Gujarat' is a work made by K.V. Narayana Rao. It is an in-depth study of the finances of the three states taking one district each. The revenue and expenditure, shares of taxes, fees and other incomes at different
levels by different authorities are analysed. The important recommendations of various committees on local finance constituted by the government of these states are also included.

The National Institute of Rural Development (NIRD) conducted studies during the years between 1978-'79 and 1981-'82 in ten states on Panchayat finance. The statistics relating to the finances of the Panchayats are given. The total receipts of Gram Panchayats in India were Rs. 113 crores; of them receipts from taxes and fees were worked out to be Rs. 39 crores. While this might average to about Rs. 5000 per Panchayat for the whole country, the average figure of Kerala was Rs. 1.1 lakhs. Even though the figures are related to a too distant past period, they throw some light on the performance of Panchayats in collecting the taxes.

In his book "Local Finance in a Developing Economy: a Study of Panchayat Finance", Karunakaran Pillai throws light on the finances of Panchayats in Kerala. It identifies the demerits of the system and gives suggestions for improved finances of Panchayats. It also points out demerits of the existing criteria for grant-in-aid and proposes to give grant-in-aid on the basis of need and fiscal capacity.

In his book 'Financial Relations between Centre States and Local Self governments in India", O.P. Sharma presented a study about the finance which
he termed as the 'Key determining factor'. The author has examined some very controversial issues relating to devolution of resources in depth. The general apathy of higher governments in giving grants and loans to the lower level governments has also been verified. The author contends that the rate of growth of economic development can be accelerated if local governments are associated with the planning process. He suggests the ways in which devolution of resources can help to achieve the economic and social objectives.

'Financing of Panchayati raj institution' is the title of the book by Ram Vinay and Prasad Singh. Here an attempt has been made to analyse the financing of Panchayati Raj Institutions with special reference to Panchayati Raj Finance Corporation. It also contains a descriptive study of the financial needs, position, structure, sources and financing in different states.

The book 'Panchayats and their Finance' by M.A. Oommen and Abhijit Datta, consists of two parts. The first part by M.A. Oommen deals with Panchayat finance and issues relating to inter governmental transfers. It reviews the structure of Panchayat finance in a historical context. It also throws light on the problems of intergovernmental transfers in the Indian federal system. The recommendations of the tenth Finance Commission have also been discussed.

The second paper by Abhijit Datta deals with Finance Commissions and restructuring of Panchayat finances. A detailed discussion of designing of
Panchayat finances, financing devolved functions, generic issues of fiscal transfer, Panchayats and plan finance and Panchayats and non-plan finance are made in this paper.

In the work titled 'Devolution of resources from the State to the PRIs,—Search for a normative approach', M.A. Oommen emphasises the need for a better sense of direction and clear evolution of objective criteria and norms for inter governmental transfer of resources. It also discusses the constitutional provisions, conformity acts, and issues before State Finance Commission.

In another work titled 'Devolution of Resources to Rural Local Bodies—a Comparative Study of Select SFC Reports', M.A. Oommen discusses mainly the constitutional tasks of State Finance Commissions and the issues relating to the expenditure and revenue assignments.

In addition to the literature reviewed above in the form of books, many articles appeared in the journals on local finance, the most important among them are given here.

The paper 'Finance for Panchayats' by Narasimham, highlights the inelastic nature of taxes collected by the Panchayats. The author opines that tax revenues are quite inadequate to meet the developmental activities of Panchayats. Taxes are not properly assessed and if they are assessed properly, it would become more elastic, the paper comments.
The paper 'Panchayati Raj and Development Finance' by Nanjudappa reviews the planning process and local finance. The achievement of targets in various sectors coming under Panchayat's jurisdiction through institutional innovation is also discussed in detail.

The impact of inflation on local government finance has been discussed by D. Greyek et al., in the paper 'The Effects of Inflation on Local Government Expenditure'. The need for adjusting the data taking in to account the inflationary rate is emphasised in the paper.

The article 'State - Panchayati Raj Financial Relation in India : an Approach', by Iyer and Hariprasad discusses at length the principles of Panchayati raj finances, various sources of revenue, various items of expenditure and the nature of relationship between the state and the Panchayats. It also makes recommendations as to how the revenue of the Panchayats could be enhanced.

A detailed study of the financial resources of the Panchayat is presented by Rao in his paper 'Resources of PRIs for Rural Development in India : Some Facts'. Each item of revenue such as taxes, fees, grants-in-aid and public contributions are dealt with in this paper. All these are analysed with reference to the different tiers of Panchayati raj.
Case study of the finance of Panchayats in Madhya Pradesh state is presented by Rao and Srivastava in the paper 'Panchayati Raj finances in Madhya Pradesh.' Available sources of finance according to the Madhya Pradesh Panchayat Act 1962 are also discussed.

"Panchayats and their finance in Kerala" is a paper by K. V. Narayana Rao. This paper elaborates the resources of Panchayats in the state of Kerala under the then constitution of Panchayats and in relation to the functions and powers of the Panchayats in the state. Analysis is made here on the basis of the data collected from all the districts.

The article titled "Local government finances: Trends, issues and reforms" by Dutta discusses briefly the local government functions and the finances against the general background prevailing in India. Local government expenditure is also discussed. It states with evidence that similar functional coverage is shown by urban and rural authorities despite their differences in functional competence. It compares the rural and urban local bodies with regard to their tax structures too. Future prospects and policy options of the local bodies are also discussed.

"Financial resources of Panchayati Raj Institution" by J. M. Girdani examines the finances of Panchayats in the context of 73rd Constitution Amendment Act, 1993. The provision of the Act with regard to the financial
aspects of the Panchayats are presented. The principles governing the fiscal transfer and the status of the Finance Commission are also discussed. Important issues of Panchayat finances are highlighted here which include the constitution of the Finance Commission leading to adequate elasticity in taxation. It also emphasises the importance of freedom to be given to local bodies for selecting their own course of development planning and funding it independently.

The paper "Flow of Funds in Panchayts Bankala During the Seventh Five Year Plan" by Pande makes a detailed enquiry of the pattern of flow of funds from various sources. It tries to verify whether the flow of fund was in consonance with local needs and priorities of the people. It also analyses the coverage especially of the poor by various programmes.

"Financial Devolution of Local Bodies, Role of the State Finance Commission" is the title of the paper by I. S. Gulati. He argues in his paper, "While for the local bodies to satisfactorily perform the functions they are assigned, they will have to have matching powers to raise funds or matching access to funds raised by the state government." He highlights the role of the State Finance Commission in ensuring that democratic decentralisation envisaged under the constitutional amendments become operational and effective. He also makes suggestions to make national level finance commission a permanent statutory body outside of the departments and ministries, with chairmanship and membership changing every five years. Once the centre takes
the initiative and puts the national level arrangements on a permanent footing, the state too could consider making similar arrangement at their level, he suggests.

Paul Bernd Spahn in his paper "Local Taxation: Principles and Scope", asserts that public service should be provided at the lowest level of government to enhance the efficiency of public sector and to increase its responsiveness to voter's preferences and demand for collective services. He observes that although guidelines to local taxation could be found in the theory of federalism their impact on actual arrangement is remarkably weak. He points out by giving illustrations that the way local services are financed in different countries varies widely. He opines that local taxation is an important part of local autonomy which is cherished by economists and political scientists alike. He summarises the main principles that govern local taxation and discusses their implications.

"Modernization of Local Government Finances and Financial Management in Hungary", is a publication in the Fiscal Decentralization Initiative (FDI) series Hungary. It is in fact a report of the conference on Modernization of local government finances and financial management held in Hungary. One of the most important conclusions drawn at the conference as per report was that the law fails to give clear and unambiguous definition of local responsibilities. Local government responsibilities and competencies are continually modified by sector related laws and state budget Acts which
generally are not co-ordinated either with each other or with the interests of local sector representative bodies, the report observes. A notable conclusion made by the conference is that the definition has a decisive impact on local body operation, but the capability to carry out their responsibilities is affected by financing methods and possibilities. Finally it puts forward a suggestion; policy makers should determine if it is better to wait for responsibilities to be assigned before changing the financing system or to begin making system changes with functions in place as at present.

"Augmentation of Panchayat Resources" is the title of the paper presented by Indira Rajaraman, O. P. Bohra and V. S. Ranganathan. The financial resources of the Panchayat raj institution in the context of the constitution (73rs amendment) Act 1993 are discussed in this paper. Analysing the current revenue and establishment and administrative expenditure of Gram Panchayat, it is argued that there is the need for additional state government resources to cover these expenditure. Five ways to augment the financial resources of Panchayat without recourse to residual assistance from higher level of government in the form of grants have been suggested. The paper argues that the revenue additionality that is required will be possible only through a detailed tax wise examination of the provisions in respect of both sharing of state level taxes and taxes leviable at Panchayat level. Incentives for local resource collection in the form of matching grant are not recommended as they do not discriminate
between variation on account of revenue raising effort and revenue raising capacity.

In the paper "Management of Panchayati raj finances in Maharashtra", an exploratory study of the finance of local bodies in Maharashtra is made by Vithal and Rao. It is a study of finances of zilla parishads as the zilla parishads were vested with the power of taxation in Maharashtra. But the study points out that the own fund of the zilla parishads constitute only less than one percent of the total receipts with grants from the state constituting a major item of revenue.

In their article "State Finance Commission and State PRI's financial relations", Sanjay Mitra and A. K. Dubey discusses the impact of the recommendations of the state finance commission on the financial relations between the state and the Panchayati raj institutions. The authors conclude the paper saying that while attempting to substantially augment the resource flow the State Finance Commissions have also sought to redefine and rationalise the various aspects of the state - Panchayati raj institutions fiscal relationship.

In his article, "Inter-governmental fiscal relations, three faces of tax sharing", S. Gurumurthi discusses three aspects of tax revenue sharing, drawing upon the international experience in the area. He puts forward the three dimensions of tax-revenue sharing, viz., tax assignment between federal and sub national governments, vertical tax revenue sharing between the federal and sub
national governments and horizontal redistribution of shared tax revenue among subnational governments. He critically examines the tax assignment options followed in various countries like Yugoslavia, Russia, China and Hungary.

M. A. Oommen in his paper, "Eleventh Finance Commission and Local Bodies - Tasks and Options" establishes that clarity of the tasks of the Eleventh Finance Commission with regard to local bodies is needed as there is no precedence to go by and local finance is no longer an appendage of state finance. The constitutional mandates and terms of reference define the tasks of the Eleventh Finance Commission. Evaluating the state finance commission reports, Oomen points out that some state finance commissions like that of West Bengal have completely overlooked the aspects of reviewing the financial position of local bodies. He also criticised the lack of seriousness with which some of the state governments have gone about the major tasks towards creating the new Panchayati raj system. Four major areas in which the Eleventh Finance Commission can take crucial decisions are also mentioned in the paper. The weak or even ad hoc pay structure for local government employees in several states also have been discussed. The major hurdle to decentralization as opined by Oommen, in this paper, has been the resistance to it by the state level bureaucracy. Creation of a Panchayat cadre to take care of rural development at the level below the district has been recommended.
"Finance commission: A quinquennial ritual?" is the title of the paper by Madhav Godbole. The Eleventh finance commission is constituted to make recommendations on certain matters one among which is the measure needed to augment the consolidated fund of a state to supplement the resources of the Panchayats in the state on the basis of the recommendations made by the State Finance Commission. He points out the drawbacks in the setting up of a commission. "The constitution does not expect the Finance Commission to work as a Finance commission of a state". He also argues that the time given to the Eleventh Finance commission is too short. He opined that serious thoughts need to be given to the question whether funds should be transferred directly from the centre to local bodies through the mechanism of the finance commission. He emphasises that the local self audit wings are too weak and are clearly not equipped to handle the tasks of audit of large funds which are being placed at the disposal of local bodies. He concludes that the emphasis in the recommendations of the Eleventh Finance Commission must not be confined to fiscal transfer, rather it must focus on promoting sound financial management by the local bodies, the states and the centre.

"Final Report for the First Local Government Conference on Fiscal Decentralization" gives a brief report of the two day conference held in July 1998 in Palestine under the auspices of World Bank. There are five sessions and many working papers were presented and elaborate discussions on the
papers were held. The conference gives many recommendations. Implementing systems and laws that regulate the relation between central government and local institutions leading to the improvement of financial situation of local bodies is one of the main recommendations. It calls for the analysis of the revenues and expenditures of local institutions so that the revenues and expenditures are equal and encourages the channeling of finances to the needed institutions.

In the paper "The Current state of local government finances and future issues : Developing a public accounting system to contribute to regional administration" it is argued that local government finance are controlled by central government.48 This control ensures a national minimum standard of public services throughout the country and prevents local governments from going bankrupt, the paper points out. But the central government control hinders the development of measures adapted to actual circumstances in the individual localities. The paper suggests to approach the local government finance in three ways for a proper understanding of local finance. Firstly, central and local government assets and liabilities must be throughly examined and non performing assets disposed off in an appropriable manner. Secondly local government activity must be rationalized through control of assets and liabilities. Thirdly redesign the institutional framework to achieve optimum distribution of management resources. It is concluded that the sources of financing are to be transferred to the local with the growing decentralization.
1.10. Reports of Government Constituted Committees and Commissions

The central government as well as the state governments have appointed a number of committees and commissions to study the financial aspects of Panchayats and to give recommendations. The central government has been taking a keen interest in the development of local bodies even though it is a state subject. The following are the various committees on financing of Panchayati raj institutions in India.

1. Local finance enquiry Committee, 1951 under the Chairmanship of P.K.. Wattal.

2. The Taxation Enquiry commission, 1953 under the Chairmanship of Dr. John Mathai.

3. Balwantray Mehta committee, 1957


The Ashok Mehta committee, 1978, The GVK Rao Committee and L. M. Singhvi Committee, 1986 also enquire into the financial aspects of Panchayats along with other aspects.

1.11. Committees Appointed by the Government of Kerala.

Government of Kerala also had constituted committees or commissions from time to time to study the financial aspects of local bodies. The following are the various committees.
1. The Taxation Enquiry Committee, 1969 under the Chairmanship of Dr. M. J. K. Thavaraj (The Thavaraj Committee).


All the above committees except Thavaraj Committee and Sen committee focused their study exclusively on Finances of local bodies. The Thavaraj Committee covered a wider area of taxation besides tax jurisdiction of the state government and local bodies. The Sen Committee was actually a committee on decentralization, but the financial aspects are also studied by the committee. The report of all these committees provide a general framework for the finances of local bodies and financial relation between state and local bodies.

The main problem felt by the local bodies as highlighted by the various commissions and committees can be understood from the words of the first State
Finance Commission. "One common thread running through almost all the reports is the mismatch between expenditure responsibility and financial resources of local bodies".49 This imbalance has been identified as the crux of the problem in local finance by various expert groups. "The Constitutional Amendment of 1992 envisage vastly enhanced expenditure responsibilities for local bodies without making any specific assignments of taxes to match the expenditure responsibilities".50

1.12 About the Study

An attempt is made here to study the rural local finance in Kerala. For that a case study of Champakulam Block, covering all Gram Panchayats under it, is made.

As all the Gram Panchayats in Kerala have been functioning under the same Act prevailing in the State and as the rules and regulations applicable to them are same, the legal framework within which they manage their finance is common. Hence a case study of Gram Panchayats in one block is made.

As it is very difficult to get the relevant data related to the finances of Panchayats from 1990 - 91 to 2000 - 01 and as the researcher has close familiarity and rapport with the Panchayats under Champakulam block, it has been selected for the case study.
1.13 Objectives of the Study

The present study aims at making an in depth analysis of the finances of Gram Panchayats. The following are the specific objectives of the study.

1. To analyse the structure and trends of revenue and expenditure of Gram Panchayats.
2. To study the disparities between Gram Panchayats in terms of revenue and expenditure.
3. To analyse the report of the State Finance Commission.
4. To examine the impact of People's Plan Campaign on Local finance.
5. To suggest measures for the better financial management.

1.14 Hypotheses

The study is based on the following hypotheses.

1. There is no significant difference between Panchayats in terms of their revenue and expenditure.
2. There is significant difference between various years in respect of revenue and expenditure of Panchayats.
3. There is a decline in the own funds of Panchayats in real terms, i.e., after adjusting for inflation, every year.
4. There is no correlation between own fund and management expenditure. Hence the own fund is not sufficient to meet the management expenditure.
5. The potential of direct taxes for yielding resources has not been exploited.
to a satisfactory level by Panchayats.

6. There is a drastic change in the pattern of revenue and expenditure during the People's Plan Campaign from that of the preceding period.

1.15 Methodology

The study is mainly analytical and partly descriptive. A deep analysis of the revenue and expenditure of the Panchayats for 11 years from 1990 - 91 to 2000 - 01 is made here. The theoretical aspects of local finance are enquired into and described here in detail. An appraisal of the State Finance Commission Report is also made.

The analytical study is based on both primary and secondary data. The secondary data form the main basis of the study. Financial data from April 1990 to March 2001 are collected from the records and accounts maintained by the Panchayats and the reports and records kept at the office of the Deputy Director of Panchayats. The eleven year period is considered to be sufficient for knowing the pattern and trends of local finance and hence the latest 11 year period for which data have been available, is included.

For collecting primary data, a schedule is prepared. Data are collected from all the members, secretaries and accountants of the Panchayats concerned. Unstructured interviews are conducted with key informants to have a clearer idea about the finances of Gram Panchayats.
A field survey is conducted in Ward III of Thalavady Panchayat to assess the building tax potential there, for comparing it with the actual. First of all, Thalavady Panchayat was randomly selected from the six Panchayats under study. Then Ward III of Thalavady Panchayat was randomly selected from all the Wards of Thalavady. A house to house visit is conducted with an expert from the Panchayat to assess the annual rental value of buildings in this ward. Based on the estimated cost of construction, depreciation and the prevailing rate of rent the annual rental value of each building is calculated. The building tax at the prevailing rate is then fixed.

The data collected are analysed electronically using statistical techniques such as proportions, averages, trend analysis using the method of least squares, index numbers including deflated indices, correlation and analysis of variance (ANOVA). Graphs and diagrams are shown for greater clarity. Conclusions are arrived at on the basis of these analyses.

1.16 Scope and Site of the Study

This is a case study of the finances of all the Gram Panchayats falling within Champakulam Block in Alleppey District. An attempt is made to study the rural local finance in Kerala. There are six Gram Panchayats in all coming under Champakulam block, viz., Champakulam, Kainakary, Nedumudy, Edathua, Thakazhy, and Thalavady. The study covers a period of 11 years from
1990 - '91 to 2000 - '01. This period includes four years of People's Plan Campaign. Hence there is scope for comparison of the finances before the People's Plan Campaign and during the Campaign. An insight into that will definitely help to understand the effectiveness and efficiency of the People's Plan Campaign. Thus the present study adds a new dimension to the existing field of knowledge. It will be useful for academic as well as practical purposes.

1.17 Profile of Panchayats

As a result of the implementation of the three tier Panchayati Raj system consequent on the Kerala Panchayat Raj Act, 1994, there were initially 990 Gram Panchayats, 152 Block Panchayats and 14 District Panchayats in Kerala. In September 2000, 19 Gram Panchayats were merged with urban local bodies and 20 Gram Panchayats were created by dividing large Gram Panchayats. Thus there are at present 991 Gram Panchayats in the state. An important feature of Gram Panchayats in Kerala is their relatively large size when compared to those in other states.

Champakulam block lies almost in the middle of Alleppey District. There are eight block divisions, eight villages and six Gram Panchayats coming under this block. Major part of the block lies in Kuttanad Taluk and a small part in Ambalappuzha Taluk. The main occupation of the people here is agriculture. The main crops are paddy, coconut, vegetables and banana. Fishing is also the occupation of a number of people. The profile of six Gram Panchayats coming
under Champakulam Block is given below.

Table 1.1
Profile of Panchayats

<table>
<thead>
<tr>
<th>Name of Panchayat</th>
<th>Grade</th>
<th>Area in sq.km</th>
<th>Number of wards</th>
<th>Population (91 census)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Champakulam</td>
<td>1</td>
<td>22.97</td>
<td>10</td>
<td>20369</td>
</tr>
<tr>
<td>Kainakary</td>
<td>1</td>
<td>32</td>
<td>12</td>
<td>20160</td>
</tr>
<tr>
<td>Nedumudy</td>
<td>1</td>
<td>25.98</td>
<td>12</td>
<td>21771</td>
</tr>
<tr>
<td>Edathua</td>
<td>Special</td>
<td>27.14</td>
<td>12</td>
<td>21715</td>
</tr>
<tr>
<td>Thakazhy</td>
<td>1</td>
<td>27.80</td>
<td>11</td>
<td>20968</td>
</tr>
<tr>
<td>Thalavady</td>
<td>1</td>
<td>15.76</td>
<td>12</td>
<td>26173</td>
</tr>
</tbody>
</table>

1.18 Contents of the Study

The thesis runs into seven chapters. In addition to the present chapter which gives an introduction to the study, literature review, objectives, hypotheses and methodology of the study, the following six chapters deal with various aspects of the study.

Chapter Two - Rural Local Finance - A Theoretical Framework and A General Overview.

This Chapter presents the general theory of local finance. Local finance in a federal system is discussed in detail. Local finance in the Indian context and the provisions under the 73rd Constitutional Amendment Act are also taken up here. An overview of the provisions of the Acts governing the finances of Gram Panchayats in Kerala is also made.

This chapter gives a brief account of the terms of reference of the Commission and the methodology and approach followed by the Commission. The analysis of the revenues and expenditures of the Panchayats made by the Commission is highlighted. This chapter examines the recommendations of the Commission. A critical evaluation of the Report is also made. Finally the response of the government to the recommendations of the Commission is given.

Chapter Four - Structure and Nature of Revenue

The composition and nature of revenue of the six Panchayats are analysed in this chapter. A composite statement of the average revenue of six Panchayats is presented. The proportions of various items of revenue to the total revenue are presented in the form of tables to explain the composition of revenue.

To throw light on the nature of revenue, each item of revenue is analysed and presented. Composite figures of all the six Panchayats as well as individual figures of each Panchayat are analysed and presented. The opinion survey analysis related to the finances of Panchayats is also included.

Chapter Five: Composition and Trends of Expenditure.

This Chapter examines the composition and trends of various items of expenditure of Panchayats. The average of each item of expenditure of
Panchayats presented in the form of table throws light on the composition of expenditure. The proportion of each item to the total expenditure is also given to explain in detail, the composition of expenditure.

The trends of various items of expenditure are also discussed based on the analysis. Another point examined is the nature of expenditure incurred by Panchayats.

Chapter Six - Local Finance under People's Plan Campaign

The finance under People's Plan Campaign is mainly analysed and discussed in this chapter. What changes have taken place in the revenue and expenditure of Panchayats during the Campaign? Are these changes drastic? What are the basic problems in local finance during the Campaign? These are some of the questions which are discussed here.

An analysis of the opinion survey, based on a schedule among the members and employees of Panchayats, related to the finances of Panchayats under the People's Plan Campaign, is also presented.

Chapter Seven - Conclusions and Recommendations

The findings of the study are presented in this chapter. The results of the testing of hypotheses are explained here. Recommendations for better finances of Gram Panchayats are also given in this chapter.
Notes and References


11. T. M. Thomas Isaac and K. N. Harilal, "Planning for Empowerment - Peoples's Campaign for Decentralized Planning in Kerala", *Economic and


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47. Final report of the First Local government Conference on Fiscal Decentralization.


