

India's eroding cooperative federalism

ASWIDELY RECOGNISED, India is quasi-federal, with powers and resources being highly tilted in favour of the Union. The Constitution provided for institutions like inter-state councils to serve as a platform for consultation between the centre and the states, and these have laid the foundation for cooperative federalism. Institutions such as the National Development Council, set up along with the Planning Commission, served to promote cooperative federalism. The 14th Finance Commission (FC) recommended a substantially higher share of the tax revenues for the states, with a clear objective to strengthen their autonomy. It also recommended the role of the inter-state council be reactivated. Even recently, when NITI Aayog replaced the Planning Commission, one of its important roles was to promote cooperative and competitive federalism.

However, in the Union's actual functioning, states' autonomy within their assigned jurisdictions, instead of being enlarged, has, in fact, been curbed. Over the years, states have come to function more as agents of the Union than as autonomous units. Here are a few examples that show how states have been coerced into accepting the Union's actions, and how the scope for states' autonomy has shrunk.

To begin with, Jammu and Kashmir, a full-fledged state, was split into two union territories at the time when there was Governor's rule and the state assembly was in suspension. This was done without ascertaining the views of the State Legislature in contravention of Article 3 of the Constitution.

The 14th FC hiked the states' share in the Centre's tax revenues by 10 ppt at one go—from the 13th FC's 32% recommendation to 42%—to promote states' autonomy in resource allocation. But, the Centre mobilised revenues by levying cesses and surcharges, not included in the divisible pool. Hence, cesses and surcharges' share in the Centre's gross tax revenues shot up to 15.7% in FY18 from 9.43% in FY12, shrinking the divisible pool of resources available for transfers to states. The divisible pool of taxes as a percentage of gross tax revenue of the

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Centre declined to 78.28% in FY20, the terminal year of the award of the 14th FC, from 86.41% in 2010-11, the initial year of the award of the 13th FC. Despite the 14th FC recommending an increase in devolution, devolution during its award period as a percentage of gross tax revenue of the Union was 34.26% as compared to 27.88% during the award period of the 13th FC.

While the total central transfer to states/UTs was ₹4.1 lakh crore in FY18, revenue mobilisation by the central government through cesses and surcharges stood at ₹3 lakh crore, or 15.70% of the Centre's gross tax revenue. This went up to ₹5.12 lakh crore in the FY20 budget estimate (BE), accounting for 21.03% of the Centre's gross tax revenue, while the total central transfers to states/UTs was ₹5.2 lakh crore. What is more, the CAG, in its reports, has highlighted the issue of underutilisation of the proceeds from cesses. It has also pointed out that the monies raised for specific purposes through some of the cesses have been diverted for other purposes by the Centre.

Following the restructuring and rationalisation of the Centrally Sponsored Schemes (CSS) in FY16, the burden on states' resources has increased considerably. Its implication is that states now have to spend more on schemes that they merely implement. To state more clearly, CSS were restructured into three categories—core of the core, core, and optional. The sharing pattern of financing between the Union and the states remained unchanged in the case of core of the core, and the contribution of states belonging to the general category was raised to 40% of the total cost of the core schemes, and 50% for optional schemes. In fact, 75.24% of the total cost of CSS falls in the category of core schemes in

the FY20 BE. To the extent the states have to contribute a larger chunk of resources to finance CSS, they lose the freedom to allocate resources on their need-based schemes.

Another example of how the states' autonomy is threatened is the additional terms of reference (AToR) given to the 15th FC. Specifically, towards the end of its tenure, the Commission was asked "to examine whether a separate mechanism for funding of defence and internal security ought to be set up and if so, how such a mechanism could be operationalised".

The ToR of a FC is constitutionally defined in Article 280(3): Distribution of the net proceeds of shareable taxes between the Union and the states and allocation among the states; the principles that should govern grants-in-aid of revenues of the states out of the Consolidated Fund of India; measures needed to augment the consolidated fund of a state to supplement the resources of the panchayats and municipalities on the basis of the recommendations made by Finance Commission of the state. Under Article 280(3)(d), the President may refer any other matter in the interests of sound finance.

Issues relating to sound budget and fiscal management have been referred to FCs starting from the 1st FC. However, AToR to the 15th FC, relating to protecting defence and internal security expenditures of the Union government, do not fit into the framework of the constitutional provision under Article 280(3)(d).

Defence is in the Union list and, therefore, the responsibility of the Union government, while internal security is largely the states' responsibility. If states

requisition paramilitary forces, they bear the expenses. It is not, therefore, an issue that should legitimately come under the domain of the Finance Commission. In any case, the original ToR itself incorporates a consideration for "the demand on the resources of the central government particularly on account of defence, internal security, infrastructure, railways, climate change, commitments towards administration of UTs without legislature and other committed expenditure and liabilities".

There could be two reasons why this AToR is added. One, the defence expenditure declined from 1.82% of GDP in FY15 to 1.54% in FY19, and is budgeted to decline further to 1.48% in FY20. As a percentage of total government expenditure, defence expenditure declined from 13.65% in 2014-15 to 11.22% in FY20. The other, with the slowdown of the economy, it could be hard to even meet this low budget provision in 2019-

20 while maintaining the fiscal deficit at 3.3%. Hence, the attempt to ring-fence the defence expenditure. Also, it could be an attempt to nudge the Commission to apportion a larger proportion of tax revenue for the Centre, leaving less in the divisible pool for states.

However, the recent implementation of the Goods and Services Tax (GST) can be cited as a remarkable act of cooperation between the states and the Union. After all, the states have agreed to give up their autonomy with respect to nine state taxes. Yet, the recent drastic cut in corporate tax, with its adverse impact on the divisible pool, and not releasing GST compensation to states falling short of the stipulated growth on time, as agreed upon, would deter the promotion of cooperative federalism.

All these examples clearly show that states' operational freedom to function within their specified jurisdictions is hugely curtailed. This is certainly not conducive to promoting cooperative federalism. Worse, they are coerced into actions that are contrary to advancing robust fiscal federalism.

The Centre is mobilising more revenue through cesses and surcharges, and it is not liable to share this with states

