

# 15th Finance Commission and Local Governments

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Panchayats have been the fulcrum of local self-government since ancient times, exercising both executive and judicial powers over village-level issues ranging from land distribution and tax collection to disputes. The enactment of the Seventy-Third and Seventy-Fourth Amendments to the Constitution formalised panchayats and Urban Local Bodies the governance system. Providing basic services at the grassroots level makes them the primary interface between citizens and the government. The article highlights the issues with the Fifteenth Finance Commission recommendations with regard to the third tier of the local governments.

**In news:** Fifteenth Finance Commission: Over Rs. 4.36 lakh crore for local governments

**Placing it in syllabus:** Law & Policy

**Dimensions**

- Recommendations on Finances for Local Governments
- Importance of the Recommendations
- Drawbacks
- Finance Commission

## **Content:**

### **Recommendations on Finances for Local Governments:**

- Finance Minister Nirmala Sitharaman accepted the 15th Finance Commission (FC)'s recommendations while presenting Union Budget 2021-22.
- The 15th Finance Commission (FC) has granted Rs 4,36,361 crore from the central divisive tax pool to local

governments, both rural and urban, for 2021-26.

### ***Quantum of Grants:***

- Of the total grant, Rs 236,805 crore is for rural bodies for local governments (Panchayat institutions) while urban bodies (municipal corporations, municipalities, etc) get Rs 121,055 crore.
- The 15th FC has also awarded Rs 106,606 crore grants-in-aid to support the health sector. The unconditional grant aims at strengthening local health infrastructure. Local bodies will get Rs 70,051 crore from it.

### ***Instituting State Finance Commissions made Mandatory precondition:***

- The FC recommend that all States which have not done so, must constitute State Finance Commissions (SFCs), act upon their recommendations and lay the explanatory memorandum as to the action taken thereon before the State legislature on or before March 2024.
- After March 2024, no grants should be released to a State that has not complied with the Constitutional provisions in respect of the SFC and these conditions

### ***Audited Accounts in Public Domain Mandatory:***

- It also recommended that, as an entry level condition, both provisional and audited accounts must be made available online in the public domain for rural and urban local bodies availing any grants.

### ***Additional Pre-Conditions for Urban Local Bodies:***

- For urban local bodies, apart from the entry level condition of having both provisional and audited accounts online in the public domain, it also suggested an additional mandatory pre-condition.
- After 2021-22, fixation of minimum floor for property tax rates by the relevant State followed by consistent

improvement in the collection of property taxes in tandem with the growth rate of the State's own GSDP will also be mandatory pre-condition.

### ***Devolution among tiers of Panchayati Raj institutions:***

- It recommended that for the five-year award period (2021-22 to 2025-26) grants should go to all the three tiers of panchayati raj institutions.
- Since no resident of India should be denied a share of the local body grants, these should be distributed to even those areas which are not required to have panchayats (Fifth and Sixth Schedule areas and Excluded Areas) for augmenting their resources to provide basic services by similar local level bodies.

### ***Grants for incubation of new cities:***

- A sum of Rs. 8,000 crore is recommended to States as grants for incubation of new cities and Rs. 450 crore for facilitating shared municipal services.

### ***Significance of Finance Commission recommendations for local government:***

- The primary task of the Union Finance Commission is to rectify the vertical and horizontal imbalances in resources and expenditure responsibilities between Union and States including the third tier of local governments.
- Part IX and Part IX-A were incorporated into the Constitution by the 73rd and 74th Constitutional Amendment.
- Part IX and Part IX-A mandate the Union Finance Commission to supplement the resources of panchayats and municipalities on the basis of the recommendations of the State Finance Commission.
- Today, more than 2.5 lakh local governments and over 3.4 million elected representatives, form the real

democratic base of the Indian federal polity.

## **Importance of the Recommendations:**

### ***Steep hike in grants to local bodies:***

- Local governments are the closest to the people at the grassroots level. They provide critical civic amenities such as roads, water and sanitation, and primary education and health.
- With this in view, the Fifteenth Finance Commission (FFC) has recommended grants of Rs 4,36,361 crore from the Union government to local governments for 2021-26.
- This is an **increase of 52 per cent over the corresponding grant** of Rs 2,87,436 crore by its predecessor for 2015-20.

### ***Inclusion of all local bodies for grants:***

- Under the 14th FC earlier, grants for local bodies included only the village Panchayat, excluding the block and district panchayats.
- It also excluded the village Panchayats in areas under the Fifth and Sixth Schedule of the Constitution.
- Similarly, for urban local bodies, it didn't make any distinctions based on population and geographical sizes. The cantonment boards in urban areas were also excluded from grants.
- However, 15th FC has included all local bodies for grants.

### ***Push for regular functioning of SFCs:***

- According to the Constitution (Articles 243-I(1) to 243-I (4)), SFCs are, at the State level, what the Finance Commission is at the level of the Union.
- As originally envisaged, Finance Commissions are to make recommendations on measures to augment the Consolidated Fund of a State to supplement the resources of local

governments on the basis of recommendations made by SFCs.

- In practice, this has not happened. Most State Governments did not constitute SFCs in time and did not give due importance to strengthening this critical constitutional mechanism.
- Even now, only fifteen States have set up the fifth or the sixth SFCs. Several States have still not moved beyond the second or third SFC
- SFCs face significant challenges in the form of poor administrative support, inadequate resources for their smooth functioning and the delayed placement of action taken reports (ATR) before State legislatures
- Making the precondition of constituting SFCs and ATR mandatory for States would help in motivating state governments to constitute these constitutional bodies.

### ***Ensuring financial accountability through conditions:***

- Auditing is necessary to ascertain the transparency and accountability of public funds and this has remained an unfinished task so far.
- The recommendations make the online availability of both provisional accounts of the previous year and audited accounts of the year before previous as entry level condition to avail of the grants.
- This will help bring transparency and accountability in local administration of public funds.

### ***Focus on metropolitan governance:***

- The 15th FC calls for a focus on urban agglomerations (UAs) that include urban local bodies, census towns and outgrowths.
- In 2011, out of the total urban population of 377 million, 61 per cent lived in UAs.
- The 15th FC has emphasised the need to focus on the complex challenges of air quality, drinking water

supply, sanitation, and solid waste management in the million-plus UAs and cities.

- Thus, for 2021-26, there is a **Million-plus Challenge Fund** of Rs 38,196 crore that can be accessed by million-plus cities only through adequate improvements in their air quality and meeting service level benchmarks for drinking water supply, sanitation, and solid waste management.
- This focus on metropolitan governance through **substantive but 100 per cent outcome-based grants** is a novel innovation.
- For ULBs other than the million-plus category, the total grants are Rs 82,859 crore.
- The grants to local governments, both urban (less than a million category) and rural, contain a mix of basic, tied as well as performance grants.

## **Drawbacks:**

### ***Reduction in performance-based grants:***

- The Fifteenth Finance Commission has reduced the performance-based grant to just ₹8,000 crore – and that too for building new cities, leaving out the Panchayati Raj Institutions (PRIs) altogether.
- The performance-linked grants were introduced by the Thirteenth Finance Commission and covered a wide range of reforms.
- The transformative potential in designing performance-linked conditionalities for improving the quality of decentralised governance in the context of indifferent states is missed.

### ***Missed opportunity to ensure minimum public services:***

- The Fifteenth Finance Commission failed to carry policy choices forward systematically.
- Articles 243G, 243W and 243ZD read along with the

functional decentralisation of basic services like drinking water, public health care, etc., mandated in the Eleventh and Twelfth schedules demand better public services and delivery of 'economic development and social justice' at the local level.

- A good opportunity to ensure comparable minimum public services to every citizen irrespective of her choice of residential location has not been taken forward in an integrated manner.

### ***Missing equalisation principle for the local government:***

- The Fifteenth Finance Commission claims that it seeks to achieve the "desirable objective of evenly balancing the union and the states".
- It is not clear why there is no recognition of the third tier in this balancing act.
- It may be relevant to recall the **Alma-Ata declaration of the World Health Organization** (1978) which outlined an integrated, local government-centric approach with a simultaneous focus on access to water, sanitation, shelter and the like.
- There is no integrated approach in the recommendations of the Fifteenth Finance Commission about the local governments (in contrast to the recommendations of the Thirteenth Finance Commission).
- Although the Fifteenth Finance Commission stresses the need to implement the equalisation principle, it is virtually silent when it comes to the local governments.

### ***Equity and efficiency sidelined:***

- The Fifteenth Finance Commission employed a population (2011 Census) with 90% and area 10% weightage for determining the distribution of grants to States for local governments.
- The same criteria were followed by the Fourteenth Finance Commission.

- While this ensures continuity, the criteria of equity and efficiency are sidelined.
- Abandoning tax effort criterion incentivises dependency, inefficiency and non-accountability.

## **Finance Commission:**

- Finance Commission is a constitutional body that determines the method and formula for distributing the tax proceeds between the Centre and states, and among the states.
- The Finance Commissions are commissions periodically constituted by the President of India under **Article 280** of the Indian Constitution to define the financial relations between the central government of India and the individual state governments.
- The Finance Commission also decides the share of taxes and grants to be given to the local bodies in states. This part of tax proceeds is called Finance Commission Grants, which is a part of the Union budget.
- The Finance Commission has a chairman and four members appointed by the President of India.

## **Functions of Finance Commission**

The Finance Commission makes recommendations to the president of India on the following issues:

- The net tax proceeds distribution to be divided between the Centre and the states, and the allocation of the same between states.
- The principles governing the grants-in-aid to the states by the Centre out of the consolidated fund of India.
- The steps required to extend the consolidated fund of a state to boost the resources of the panchayats and the municipalities of the state on the basis of the recommendations made by the state Finance Commission.
- Any other matter referred to it by the president in the



interests of sound finance.

- The Commission decides the basis for sharing the divisible taxes by the centre and the states and the principles that govern the grants-in-aid to the states every five years.
- Any matter in the interest of sound finance may be referred to the Commission by the President.
- The Commission's recommendations along with an explanatory memorandum with regard to the actions done by the government on them are laid before the Houses of the Parliament.
- The FC evaluates the rise in the Consolidated Fund of a state in order to affix the resources of the state Panchayats and Municipalities.
- The FC has sufficient powers to exercise its functions within its activity domain.
- As per the Code of Civil Procedure 1908, the FC has all the powers of a Civil Court. It can call witnesses, ask for the production of a public document or record from any office or court.

**Mould your thought:** Recommendations and innovations of the 15th Finance Commission could catalyse progress in the accountability and effectiveness of local governments in India. Evaluate.

***Approach to the answer:***

- Introduction
- Discuss the recommendations of 15th FC for local bodies in brief
- Discuss the importance of these recommendations
- Discuss the drawbacks
- Conclusion