Concerns on State Finance Commissions

What is the issue?

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States have not been setting up their State Finance Commissions(SFC) every five years as mandated by the 73rd Amendment Act, 1992.

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What are its constitutional mandate?

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- The state finance commissions were added by 73rd amendment act.
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- They have been enshrined in article 243-I and 243-Y in Part IX A and IX B and are constituted by Governor every five years.
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- Their Primary concern is to suggest ways and means to strengthen the institutions of local governance. (Panchayati raj institutions and Urban local bodies)
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- They recommend principles and methodology as regards the devolution of funds to PRI's and ULB's.
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- The recommendations of the state finance commissions include:
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1. The distribution between the State and the local bodies of the net proceeds of the taxes, duties, tolls and fees leviable by the State.
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2. Determination of the taxes, duties, tolls and fees levied or appropriated by the local bodies
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3. The grants-in-aid to the local bodies from the Consolidated Fund of the State
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4. Measures needed to improve the financial position of the local bodies

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- The governor is required to place every recommendation made by the SFC and actions taken by the state governments on it before the state legislature.
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What are the concerns?

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- There are many cases where the recommendations of an SFC have neither been formally accepted by the State government, nor was the SFC report laid before the State legislature.
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- There are also instances where the State government, despite having accepted its SFC's recommendations fully or partially, has not implemented them.
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- These developments have affected empowerment and finances of local bodies.
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- States like Manipur witnessed a gap prevailed between the recommendation of successive SFCs and the State government's actual fund transfer to its hill districts' local bodies.
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- It results in accentuating the grievances of hill tribes against their counterparts in the plains.
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What is the role of central finance commissions?

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- Central finance commissions, while recommending on the overall devolution from the central pool of divisible resources to the States, factor in recommendations given by SFC to their respective states.
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- The 14th FC had recognised that governing cities is becoming a major challenge because of shortage of finances, weak institutional framework and lack of capacity for service delivery.

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- It observed that the rural local bodies were in many cases not equipped to perform their core functions.
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- It recommended a total devolution of Rs.2,87,436 crores for all the local bodies, constituting an assistance of Rs.488 per capita per annum at an aggregate level.
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- The present 15th Finance Commission (FFC) is also tasked “to consider provision of grants-in-aid to local bodies for basic services, including quality human resources, and implementation of performance grant system in improving delivery of services”.
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- The FFC has to recommend specifically the amount to be devolved to the States during its award period (2020-25) for local bodies.
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What should be done?

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- As per the existing system, all funds devolved to States on recommendations of CFC are directly transferred to State governments’ treasuries.
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- The Fifteenth Finance Commission should recommend that the funds earmarked for PRIs and ULBs, should be managed through **public financial management system**.
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- It would track flow of funds on a real-time basis and will eliminate delays in transfers to local bodies.
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- A portion of the earmarked funds for PRIs and ULBs could be distributed as **incentive** to States which constitute their SFCs as per the constitutional norm.
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- This should empower them to raise tax and non-tax revenue in areas specified by FFC and SFCs.
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- Local bodies of States performing better will gain, which should induce the other State governments to be more conscious of their responsibilities.
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- Local bodies are the interface between State institutions and the public towards obtaining basic services.

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- Hence, the 15th Finance Commission must incentivise the States to constitute their SFCs and empower their local bodies.
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- The role of governors is also crucial as a benevolent institution of oversight and ensuring vibrant functioning of local bodies.
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Source: Business Line

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