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Lesson No.

- 2.1 Ministry of Finance : Organisation and Working
- 2.2 Finance Department of Punjab : Organisation and Functions
- 2.3 Finance Commission : Composition and Role
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Department website : www.pbidde.org

MINISTRY OF FINANCE : ORGANISATION, STRUCTURE AND WORKING

The Finance Ministry is considered to be one of the most important Ministries in the Union Government. Finance is the fuel for the engine of administrative machinery and finance is managed by the Finance Ministry. This ministry exercises great control over the working of all other departments. It keeps the administrative machinery on its wheels by providing money for expenditure to the various departments. The Finance Ministry is headed by the Finance Minister who is a very important member of the Cabinet.

The origin of the Ministry of Finance can be traced to the year 1810, when a separate Department of Finance was first set up in what was then called Supreme Government of India. In 1883, with the reorganisation of Supreme Government, finance was one of the four departments, the other three being Military, Foreign and Home. After independence in 1947, the Department of Finance was redesignated as the Ministry of Finance. It consisted of three wings, namely, Expenditure, Economic Affairs and revenue. The number of departments in the ministry has undergone changes several times with as many as five departments (Revenue, Expenditure, Economic Affairs, Coordination and Company law and Insurance) in 1963, and as few as two departments (Revenue Expenditure and Economic Affairs) in 1949. At present, the Ministry of Finance is organised into four departments: (i) Department of Economic Affairs, (ii) Department of Expenditure, (iii) Department of Revenue, (iv) Department of Disinvestment. Each of these four departments is headed by a full-fledged secretary. But one of them looks after coordination and administration and thus may be said to be first among equals. This role is performed by the Secretary in the Department of Economic Affairs.

ORGANISATION OF THE MINISTRY OF FINANCE

The Ministry is headed by a Cabinet Minister who is assisted by one or more Ministers of State. The administrative head of the Ministry of Finance is the Finance Secretary and there is a full-fledged Secretary in charge of each of the four departments (i.e. Department of Economic Affairs, Department of Expenditure, Department of Revenue and Department of Disinvestment). Secretaries of each of the four departments are assisted by Additional Secretaries, Joint Secretaries, Deputy Secretaries, Directors, Under Secretaries and Secretarial Staff under them. Most senior administrative posts in the Ministry are held by officers belonging to the IAS (Sometimes non IAS officers are appointed as was the case when Bimal Jalan and

Montek Ahluwalia were appointed as the Finance Secretary and his resulted in immense resentment among the IAS Cadre Since the post of Finance Secretary is a crucial one and carries with it an informal 'Veto power over the proposals for expenditure emanating from other ministries and departments)

The Ministry of Finance also draws officers from other services such as the Indian Audit and Accounts Service the Central Revenue Service of the Central Customs and Excise Service the Indian Railways Accounts Service and the Central Secretariat Service at various levels.

The Ministry of Finance is presently organised into the following departments:

- (i) Department of Economic Affairs
- (ii) Department of Expenditure
- (iii) Department of Revenue, and
- (iv) Department of Disinvestment
- (v) Department of Financial Services

DEPARTMENT OF ECONOMIC AFFAIRS

The Department of Economic Affairs monitors economic trends in the country and advises Government on all matters, having a bearing on internal and external economic management, including the working of commercial banks, term-lending, institutions, investment regulations, external assistance etc. It is also responsible for the preparation of the Budget of the Union Government, as also Budget of States under President's Rule

The Department of Economic Affairs (DEA) works under the overall supervision of the Secretary, Economic Affairs, who in turn is assisted by a Special Secretary, an Additional Secretary an number of Joint Secretaries and Economic Advisors as well as consultants.

This Department comprises of the following Divisions:

- (i) Economic Division
- (ii) Banking Division
- (iii) Insurance Division
- (iv) Budget Division
- (v) Capital Market, External Commercial Borrowings and Pension Reform Division
- (vi) External Finance Division
- (vii) Currency and Coinage Division'
- (viii) Aid Accounts and Audit Division
- (ix) Administrative Division

(I) Economic Division—The Economic Division is the nodal wing of the Ministry of Finance attending to all economic policy matters affecting the country. The Division monitors economic policy and advises on policy measures relating to macro

management of the economy and on reforms. Its Important functions include analysis of events of economic importance and research study on economic problems.

(II) Banking Division—The Banking Division of this Department deals with policies having bearing on the working of commercial banks and term lending institutions excluding Life insurance Corporation of India

(III) insurance Division—The Insurance Division exercises control and supervision over the activities of the (Nationalised) insurance industry both Life and General Insurance. The functions of this Division includes policy formulation and administration of the insurance industry, review and monitoring of the performance of Insurance companies, framing of rules and regulations in respect of service conditions of employees of nationalised insurance companies.

(iv) Budget Division—The Budget Division has the responsibility of preparing the Central Budget (other than that of Railways) and supplementary and excess grants for presentation to the Parliament and obtaining the Parliament sanction for the same. It does the same for states and Union Territories (with legislatures) under President's Rule. This Division is responsible for monitoring the fiscal position of the Union Government.

(v) Capital Market, External Commercial Borrowing and Pension Reform Division—The Capital Market, External Commercial Borrowing and Pension Reform Division keeps an eye on the stock exchanges as the securities law, (Amendment) Act, 1999 and (repeal of 1969 notification has permitted trading in derivatives which has commenced on the BSE and ONSE from June 2000.

(vi) External Finance Division—The External Finance Division, as its name suggests, deals With matters relating to financial assistance received by India from sources abroad, such as International Monetary Fund (IMF), the World Bank the Asian Development Bank, International Developments Associations, International Finance Corporation (IFC). Multi lateral Investment Guarantee Agency (MIGA) etc. All proposals in regard to trade and payments agreement with foreign countries as well as broader questions of policy in regard to foreign trade are examined in this Division.

(vii) Currency and Coinage Division—There are ten industrial organisation's under the administrative control of Currency and Coinage Division. Out of these five are Mints, two note printing presses, two security printing presses and one paper mill.

(viii) Aid Accounts and Audit Division—The Aid Accounts and Audit Division, which is the part of the External Finance Division of the Departments of Economic Affairs is responsible for various functions relating to external loans/grants obtained by the Government of India from various multi lateral and bi-lateral donors In addition this Division carries out audit of import licences issued ,to registered exports for export promotion

(ix) Administrative Division—The Administrative Division is responsible for personnel and office administration- of the Department of Economic Affairs. This Division looks after administrative [and vigilance matters concerning the department, as well as its attached and subordinate offices

DEPARTMENT OF EXPENDITURE

Department of Expenditure controls the entire expenditure of the Central Government. This Department is concerned with expenditure related financial policies of the Government financial rules and regulations and delegation of financial powers, review of staffing in Government establishments, general principles of government accounting, administration of central treasury rules, state finance. Plan, budget planning and development finance, capital restructuring of public sector undertakings,

Indian Audit and Accounts Department etc. This Department functions through the following Divisions.

- (i) Establishment Divisions
- (ii) Plan Finance Division
- (iii) Cost Account Branch
- (iv) Staff Inspection Unit
- (v) Defence Division
- (vi) Comptroller General of Accounts
- (vii) Civil Expenditure Division

(i) Establishment Division—The Establishment Division administers financial rules and regulations including those relating to the conditions of service of Central Government Employees.

(ii) Plan Finance Division—The Plan Finance Division deals with state plans for economic development It advises on proposals of state governments for investment in industrial enterprises irrigation, power and flood control projects. It conducts studies on state taxation and budgets

(iii) Cost Accounts Branch—The Account ounts Branch (CAB) is a specialized pricing office of the Government within the Ministry of Finance Department of Expenditure. It deals with all cost accounting work arising in the various department.

(iv) Staff Inspection Unit—The Staff Inspection Unit was set up in 1964 with the object of effecting economics in manpower consistent with administrative efficiency and evolving performance standards and work norms in the Government offices and ins 'tutions wholly or substantially dependent on Government grants.

(v) Defence Division—The Defence Division renders financial advice to the Defence Head Quarters, the Defence Ministry and to the officers directly subordinate to the Ministry. This Division is responsible for scrutiny, sanction and accounting of the

expenditure of the Defence Ministry.

(vi) Comptroller General of Accounts—The Comptroller General of Accounts is the apex accounting authority of the central government exercising the powers of the President under article 150 of the Constitution for prescribing the form of Accounts of the Union and State Governments on the advice of Comptroller and Auditor General of India.

(vii) Civil Expenditure—There are ten Civil Expenditure Divisions each headed by an Additional secretary or a Joint Secretary In addition to rendering financial advice to the Ministries Departments of the Government of India. Officers of these divisions also function as financial representatives of government on Board of Directors of various public sector undertakings and on governing bodies of autonomous organizations which receive substantial financial assistance from government.

DEPARTMENT OF REVENUE

The Department of Revenue functions under the overall administrative direction and control of the Secretary (Revenue). It exercises control in respect of matters relation to all the Direct and Indirect Union Taxes through two statutory Boards, namely, the Central Board of Direct Taxes (CBDT) and the Central Board of Excise and Customs (CBEC) Each Board is headed by Chairman who is also ex officio special secretary to the Government of India. Matters relating to the levy and collection of all the direct taxes- looked after CBDT. whereas those relating to levy and collection of custom and central excise duties and service tax fall within the purview of CBEC the two boards were constituted under the Central Board of Revenue Act 1963. CBDT has six members and CBEC has five members. The members are also ex-officio Additional Secretaries to the Government of India.

Some of the important Divisions of the Department are given below:-

Narcotics Control Division deals with framing of annual opium licensing policy, notifying track for cultivation of opium poppy in pursuance of opium licensing policy, matters relating to poppy straw and poppy seeds fixation of procurement price of opium payable to poppy cultivators, matter relation to Central Bureau of Narcotics.

Sales Division deals with enactment and amendment of the Central Sales Tax Act and the Indian Stamp Act, 1899 and levy of tax on sales in the course of inter state trade or Commerce VAT etc.

Economic Security Cell has been recently constituted in this department of look after all matters relating to economic intelligence including coordination with various ministries and national & international . Organisations/agencies in matters relating to economic crimes. The cell also looks after matter relating to financing of terrorism which is being coordinated by MHA.

DEPARTMENT OF DISINVESTMENT

The Ministry of Disinvestment was converted into a Department under the Ministry of Finance with effect from 27th May 2004 and has been assigned all the work relating to disinvestment, which was earlier being handled by the Ministry of Disinvestment.

This Department was assigned the following works:-

- (a) All matters relating to disinvestment of Central Government equity from Central Public Sector Undertakings
- (b) Decisions on the recommendations of disinvestment Commission on the modalities of disinvestment, including restructuring
- (c) Implementation of disinvestment decisions, including appointment of advisors, pricing of shares, and other terms and conditions of disinvestment
- (d) Disinvestment Commission, (consequent upon change in the policy of the Government the term of Disinvestment Commission was not extended further and it was wound up with effect 31st October, 2004)
- (e) Central Public Sector Undertakings. for purposes of disinvestment of Government equity only.

Some of the important initiatives taken are given below:-

The disinvestment of Government equity in Public Sector Enterprises will be carried out in accordance with the policy laid down in the National Common Minimum Programme

Government has decided, in principle, to list large profitable Public Sector Enterprises (PSE's) on domestic stock exchanges and to selectively sell a minority stake in listed profitable PSEs while retaining atleast 51% of the shares alongwith full management control so as not to disturb the public sector character of the companies

Government has also decided to constitute a National Investment "Fund" into which the realization from sale of minority shareholding of the Government in profitable PSEs would be channelised. The Fund would be maintained outside the Consolidated Fund of India. The income from the fund would be used for the following broad investment objectives—

- I Investment in social sector projects which promote education, healthcare and employment.
- II Capital investment in selected profitable and revivable Public Sector Enterprises that yield adequate returns, in order to enlarge their capital base to finance expansion/diversification

DEPARTMENT OF FINANCIAL SERVICES

This Department has been added recently to the Ministry of Finance It consists

of two Divisions, namely, Banking and Insurance Divisions. The Banking Division—Administers Government policies having a bearing on the working of public sector banks and the term lending Financial institutions.

The Insurance Division—All policy issues relating to Life Insurance and General Insurance in the country, including Insurance Regulatory Authority, fall within the domain of this Division

FUNCTIONS AND ROLE OF THE MINISTRY OF FINANCE

The Ministry of Finance/Finance Department is always responsible for the entire financial administration of the country. The Ministry performs a variety of functions with regard to finances of the country. It has control over expenditure of money. It controls and coordinates various spending departments of the government. It is responsible for the collection of the taxes and it exercises vital control and supervision over the expenditure of the government departments. More recently, with the addition of a new 'Department of Disinvestment' to the Ministry of Finance its spectrum of functions has further widened to encompass all matters relating to disinvestment of central Government equity from central public sector undertaking. Thus, Ministry of Finance is responsible for the following functions-

- (a) Administration of the finances of the Central Government and handling of financial matters affecting the country as a whole.
- (b) Raising the necessary revenues for carrying on the administration and planning the taxation and borrowing policies of the government.
- (c) Administration of problems relating to banking and currency and in consultation with the Ministries concerned, arranging for the proper utilisation of the country's foreign exchange resources.
- (d) Controlling the entire expenditure of the Government in cooperation with the administering ministries and departments concerned.
- (e) Dealing with all matters relating to disinvestment of Central Government equity from Central public sector undertakings.

Conclusion:-

The ministry of finance is the most important ministry among the ministries of central Government. It exercises its control over all other ministries; it prepares the financial statement of the country and such it serves as the custodian of national exchequer.

BOOKS

- MJ.K.Thavaraj - Financial Administration in India
- M.P. Sharma - Public administration in theory and practice
- Sahib Singh/Sawinder Singh - Public Personnel & Financial Administration

www.finmin.nic.in

PUNJAB FINANCE DEPARTMENT

Finance is the fuel for the engine of Public Administration. Mr. L. George is reported to have once remarked that “Government is Finance.” This is quite correct, because for almost everything that Govt. does require money. Even the best conceived policies and plans will come to light only if funds are available to pay the personnel and purchase the equipment and the materials required. The importance of Finance to administration is thus obvious. Finance and administration are closely intertwined in three ways. In the first place, most administrative acts have their financial implications. They create a charge on the public exchequer or bring revenues to it. In the second place, Financial operations may be designed to develop and promote particular public policies, e.g. tariffs may be so shaped as to afford protection to the home industries, or money from the rich to the poor. Thirdly and finally, Financial administration raises important issues of administrative organisation and relationship. e.g.. machinery of Financial Administration its relationship with administrative authorities. Financial administration consists of those operations, the object of which is to make funds available for the Government activities and to ensure the lawful and efficient use of these funds. Under democratic Govt., the Legislature is the body to vote the taxes and authorise expenditure. Financial administration has to see that the legislature is not asked to place more tax burden on the people than is necessary and that the money voted by it for expenditure is used according to its wishes and with due regard to economy and efficiency. In brief, we conclude the importance of Finance in the words of famous political philosopher like W.E. Gladstone, “The Finance of the state is ultimately associated with the liberties of the state. Now, we are going to discuss Finance Department of Punjab.

The Constitutional requirement on the part of the Governor under Article 202 of the constitution to present Annual Financial Statement before the State legislature lies with the responsibility of Finance Department. Although the Finance Department adheres strictly to financial rules and regulation in all the matters. It is very rarely that it makes departure in very exceptional cases or circumstances so as to avoid creating embarrassing precedents.

As the Finance Ministry at the Union level, so is the Finance Department at the State level is the nucleus round which financial administration of the State concerned revolves. It controls not only the finance of State government but also regulates financial matters affecting the State as a whole. However, the organisation and functions of a Finance Department differ from state to state in India.

Organisation of Finance Department of Punjab : Each department in Punjab is headed by Cabinet Minister as its Political head and by Secretary as administrative head. Likewise, the Department of Finance is also organised similarly and is the premier department. The Secretary is assisted by a special Secretary Finance. He is further assisted by Joint Secretaries, and Deputy Secretaries- three each and Under Secretaries- four in number. All of them held independent charge of one or more different subjects.

It is, however, interesting to note that the branches dealing with finance. personnel are directly answerable through the head of the Branch to the Chief Secretary in matters relating to transfers, promotions and other conditions of service. The Deputy Secretary or Under Secretary responsible for the functioning of these branches can deal directly with the office of the Chief Secretary without routing cases through the Finance Secretary. The advice of the Finance Secretary may also be had in case there is need for it.

Functions of the Finance Department: The functions of the Finance Department can be discussed under three heads as follows:

The fundamental right of legislature under any responsible form of government is not only to ensure that public funds are revised with its consent but also to exercise complete control over the way in which the nation's revenues are spent by the government. It is through financial committees that the legislature ensures that its control over finances is fulfilled. The legislature as a general body is too large to exercise any specific control over public expenditure. It is therefore, left to the Committees to act as the legislature in keeping a strict watch over public purse.

1. Functions relating to Expenditure: Functions relating to expenditure can be studied as :

(i) Custodian of Public Revenue : The Finance Department is the custodian of public funds. Its first and foremost function at the time a new post is to be created or hike in salary is to be made is to scrutinise the impact it will have on public revenue. Such proposals may originate any time-at the time of preparation of budget or during the course of a Financial year. Any such proposal is required to be sent to the F.D. indicating: (a) urgency in respect of the proposal submitted, (b) details of the estimated additional expenditure & loss of revenue, except in the case of building schemes for which sketch plans and approximate estimates are generally considered sufficient. It

is up to the Finance Department to accept or decline sanction after scrutiny. Proposals involving recurring expenditure such as increase in establishment, are examined very carefully. It is availability of funds which, determines ,as to which of the schemes may be sanctioned.

(ii) Adherence to Financial Rules and Regulations: The F.D. adheres strictly to financial rules and regulations in all the matters. It, is very rarely that it makes departure in any exceptional cases, circumstances so as to avoid creating embarrassing precedents.

(iii) Co-ordination: Different departments have their perception on a particular matter and may send a proposal, likewise. But it is for the Finance Department to secure co-ordination. For instance, a particular department may send a proposal for enhancement in the salaries of different categories of staff working under them'. It is for the F.D. to see what financial implications it will have on other departments and take decision accordingly.

2. Functions relating to Revenue: In view of the magnitude and complexities involved, the administration of revenue is entrusted to the Administrative Department concerned. So, there is negligible control of the Finance Department in this field. Still, the F.D. performs following functions:

- (i) It receives periodical reports about the progress of the collection of revenues.
- (ii) It may advise, steps to be taken in this regard.
- (iii) It may examine methods employed in the process of collection of revenue and suggest methods for improvement.
- (iv) It may issue directions with regard to matters involving grant of land or assignments of revenue or concession, grant lease or licence of mineral or forest right or a right to water, power or any easement of privilege in respect of such concession, or any relinquishment of revenue for which credit has been taken in the budget.

3. Functions relating to Miscellaneous Matters:

(i) Preparation of State Budget: The Constitutional requirement on the part of the Government under Art. 202 of the Constitution of present Annual Financial Statement before the State Legislature is in fact responsibility of the Finance Department for consolidation in the form of budget.

Budgetary Discussion: The function of each and every department of the government comes under close scrutiny at the time the demand for that department as provided in the Budget come under discussion of the legislature. It is a time when every kind of question can be raised regarding the functioning of the department

concerned. Questions of policy, economy, grievances, complaints etc: are usually raised and the minister concerned has to give a satisfactory reply. It is however, a few days after the budget has been presented to the House the general discussion taken place on it. The budget is presented to the Vidhlian Sabha usually at 5 P.M. on the last day of February by the Finance Minister with_a budget speech. There is no discussion on that day. At the time to general discussion, the house shall be at liberty to discuss the Budget as a whole on any question of principle involved therein, but no motion shall be moved nor shall the budget be submitted to the vote of the House.

Voting of Demands : When the general discussion of the Budget is over, the Vidhan Sabha proceeds to voting of Demands for grants that is voting of the Expenditure part of the Budget. The demand is made in a motion. A demand when duly voted becomes a grant To these demands, three kinds of cut motions can be moved to reduce the amount of demand in any of the following ways:-

- (a) Policy cut motion
- (b) Token cut
- (c) Economy cut

(ii) Ensure Availability of Cash: It is the responsibility of the Finance. Department to ensure availability of funds throughout the year not only for meeting expenditure on various departments but also for transaction relating to debt, deposit and remittance in expenditure. It has to see that a minimum balance is maintained with the Reserve Bank and with the treasuries for meeting expenditure.

(iii) Watchman of Progress of Expenditure : The F.D. is also a watchman of the progress of expenditure. It maintains watch that expenditure sanctioned on particular schemes and under particular needs is being incurred proportionately. It means that with in six months expenditure incurred must be in the tune of 50 percent of the total sanctioned and should not happen that whole of the sanctioned amount or a very little proportion there of is to be incurred at the end of the financial year.

(iv) Agent of the Central Government: The F.D. play the role of an agent of the central government in cases where certain Administrative Departments are entrusted with the responsibility to prepare budget estimates in certain subjects administered by them on behalf of the central government. Hence, the respective Administrative Department has to address the finance department if any amendment is considered necessary on the basis of any instructions received by them from the central government.

(v) Consultation on Taxation Proposals: The policy of taxation concerns the respective Administrative Department. But the F.D. has to be consulted in all proposals for a increase or decrease of taxation as financial implications thereof are to be scrutinised

by it.

(vi) Raising Public Loans: Article 293 of the Constitution entitles the State Government to raise loans within the territory of India upon the security of the Consolidated Fund of the State within such limits as may be fixed by the legislature from time to time. However, in practice, this responsibility lies with the F.D.

(vii) Action on Recommendations of Public Accounts: It is the responsibility of the F.D: to see the Recommendations of the Public Accounts Committee and the Legislative Assembly are duly considered and the orders passed on them are communicated to the Accountant General. A statement showing the action taken each years on such recommendation and incorporation ill its next report.

(viii) Responsible for Audit of Local Body Accounts: The F.D. is responsible for conducting audit of the accounts of local bodies.

Audit, like the judiciary, the executive and the legislature is one of the important ingredients of democracy: Audit is conducted by an independent constitutional authority known as the Comptroller and Auditor General of India. Under him are one Accountant General at State level and one Accountant General (Revenues) for auditing accounts of the states respectively. These all submit the annual statements of Audit based on a particular financial year pointing out financial irregularities and lapses on the part of various departments if any. This report is presented before the state legislature. Further action calling for explanation of the head of the department concerned lies with the Public Accounts Committee, which has on it members of almost all political parties. It is then, through the Finance Department of the State concerned that necessary replies are sent to the respective Accountant General.

In this way, we find that not only is the passage of Budget necessary but also that proper control should be maintained by the legislative over the executive which utilises it for performing public policies laid down. Money is such an element which needs proper control for its utilisation, otherwise. irregularities are bound to occur here and there. It is with this relations that the legislature exercises control over the executive while passing the Budget and even it has been passed and being executed.

Conclusion :- There is no denying the fact that Finance Department has its responsibility for financial control. Actually, it is Finance department which exercise overall control over all the departments so far as the financial aspect is concerned. Moreover, it is solely concerned with exercising this control through Budgetary Process.

In brief, Finance Department controls and coordinates various departments that incur expenditure. Moreover, the making of general financial and economic policies and programmes of government is the responsibility of Finance Department.

Although it prepares estimates of income and expenditure and submits them to the Legislature for approval. After Legislature has approved, the Finance Department plays the most important part in the execution of financial matters. As such, it is a department of control and supervision whose main duty is to manage finances of the state.

SUGGESTED BOOKS

1. *Finance Commission-and Centre-State Financial Relations in India.* by S.S. Janjua.
2. *Fiscal Federalism in India* by R.K. Sinha.
3. Financial Administration : Thavaraj
4. Financial Administration : Sahib Singh, Swinder Singh
5. Theory and Practice of Public Administration : M.P. Sharma

**FINANCE COMMISSION IN INDIA : COMPOSITION,
FUNCTIONS AND RECOMMENDATIONS OF
FINANCE COMMISSIONS**

This strong centre and the weak states arrangement was introduced intentionally by the framers of the Constitution in a bid to stall the divisive forces operating in the economy. However, certain developments in the political field have considerably eroded independence of the states and their political and economic powers. Therefore, quite recently, demands for increase in state autonomy have been raised by various quarters. While no one denies the importance of a strong centre for preserving the integrity of the nation, it is necessary to give a serious thought to these depends. Grant of certain amount of autonomy atleast, in the sphere originally contemplated by the Constitution, is necessary to fulfil the democratic ambitions of the people.

In brief, actually the transfers through the Finance Commission which is statutory body contribute only about 1/3 of total transfers from the centre to the states. This means that about 2/3 of the transfers are channelled through the Planning Commission or the Central Govt. directly. Since the centre contributed a large amount of resources in the form of discretionary grants to the states, acquired considerable powers to effect the decision-making processes at the state level. This led to further erosion of autonomy of the states.

Finance Commission

An Introduction :- Article 280 of the Indian Constitution stipulates the setting of an independent agency called Finance Commission with a view to making recommendation in regard to the distribution of the net proceeds of taxes and its allocation among various States and the principles which should govern the grants in-aid to the States out of the Consolidated Fund of India: It is said that the President of India within a period of two years of the commencement of the Constitution and there after at the expiration of every fifth year, or at such earlier time as he may deem necessary will constitute this Commission consisting of a Chairman and four other members. The Parliament has been authorised today down their qualifications and the mode of selection.

Finance Commission Act :- In accordance with the Constitutional provision, the Finance Commission Act was passed in 1951. As amended in 1955, the Act lays down that the Chairman shall be appointed from amongst persons who had experience of affairs and the other four member shall *be* selected from amongst persons who are, or have been, or are qualified to be appointed as judges of the High Court, or have special knowledge of the Finances and accounts of the Government, or have had experience in financial matters and administration, *or* have special knowledge *of* economics. However, before appointment is made, the President shall satisfy that the person concerned will have *no* such financial *or* other interestes as is likely *to* affect prejudicially his functions as a member *of* the *Commission*. The Act further lays down that the *Commission* shall determine its own procedure and in the *performance of* its *functions* shall have the powers *of* a civil *Court*. It shall have the powers to require any person *to* finish information which may be essential for its working.

Functions of the Finance Commission :- The Commission shall recommend *to* the President as *to* :

- (a) the distribution between the Union and States of the proceeds of taxes which are *to* be, ar may be, divided between them and the allocation between States af the respective shares af such proceeds;
- (b) the principles, which should govern the grants-in-aid of the revenues of the State out af the Consolidated Funds Of India; and
- (c) the continuance of modification of the term of any agreement entered into by Govt of India with the states.
- (d) any other matter referred to the Commission by the President in the interest of a sound finance.

It is also written that the President shall cause every recommendation made by the Finance Commission together with an explanatory note detailing the action there on to be laid before each House of Parliament.

A detailed study of the Constitution establishes that the functions of the Finance Commission are not exhausted merely by Article 280. For example, Article 270 makes it mandatory to divide taxes, on income, other than agricultural, between The Union and the mandatory to divide taxes, on income other than agricultural, between The Union and the States. In so far as income tax is concerned, the Finance *Commission will recommend*.

- (a) the percentage of the proceeds of taxes on income excluding the taxes payable in respect of the emoluments of the Central Government that shall be deemed to represent proceeds attributable to the Union Territories; and
- (b) the percentage of the net proceeds in any financial year of tax on income other than agricultural income, except in so far as these represent proceeds attrib-

utable to the Union Territories or taxes payable in respect of the emoluments of the centre that shall not be taken to form part of the Consolidated Fund of India but shall be assigned to the State within which the tax is leviable in that year and the manner in which and the time from which such percentage shall be distributed among the State Governments.

The President is also authorised under Article 280 (3) clause (c) to refer any matter to the Finance Commission that he may deem necessary in the interest of 'sound finance'. The President, under this provision, had asked the Commission to make recommendation in regard to the principles that should govern the distribution of the net proceeds among the States in a financial year in regard to the estate duty in respect of property other than agricultural land, tax or railway fare and additional duties of excise on mill made textiles, sugar and tobacco.

So far Eleven Finance Commissions has been constituted by the President of India in: 1951, 1956, 1960, 1964, 1968, 1972, 1977, 1982, 1987 and 1992. 11th Commission gave its report in 2000.

Eighth Finance Commission :- The President constituted the eighth Finance Commission on June 20, 1982 under the Chairmanship of Y.B. Chavan. It submitted its report in May, 1984. It recommended that:

1. 85% of the proceeds of Income Tax, excepting the portion representing the proceeds attributed to Union territories, be distributed among the states (as under the previous provisions).
2. The Share of the States in Union excise duties (excluding duty on electricity) be raised from 42% to 45%.
3. The entire net proceeds of the additional excise duties on sugar, textiles and tobacco; excluding the portion attributable of the Union territories, should go to the States.
4. In ten states, assessed to be in deficit after devolution, be given grants to make up. These states are Assam, Himachal Pradesh, J & K, Manipur, Nagaland, Orissa, Sikkim and West Bengal.
5. Debt relief to the States varying from 20 & 85% of non-plan capital gap be given.

These recommendations involved a transfer of approximately 38,500 crores to the States by way of devolution of taxes, duties and grants-in-aid during the five year period, 1984-89 as against transfer of Rs. 21, 000 crores during the proceedings five years as recommended by the Seventh Finance Commission.

Ninth Finance Commission :- The President constituted the Ninth Finance Commission on June 17, 1987 under the chairmanship of N.P. K. Salve, M.P. and Former Union Minister of State, to go into the question of distribution of non-plan resources

between the Centre and the States.

The terms of reference of the Ninth Finance Commission are probably the widest ever given to any Finance Commission so far. The Commission, in its report, pointed out that “the fiscal scenario in the *country* has gradually worsened to an alarming extent.” So, “in the light of this continuing deterioration of the fiscal situations eliminating the revenue deficits as early as possible in an absolute fiscal imperative.” the Commission set before itself the specific task of “phasing out the revenue deficits during the next six years so that by the end of the fiscal year 1994-95 the Centre and the States would be balancing their revenue accounts.”

The Commission recommended that :

A sum of Rs. 13,662.42 crores may be transferred to the States from the taxes collected by the Union Government during 1989-90 against a proposed sum of Rs. 10,682 crores during 1988-89. Uttar Pradesh being biggest State in terms of population has been allocated maximum share of Rs. 2,163.42 crores terms of population has been allocated maximum share of Rs. 2,163.42 crores against Sikkim, the least populated State with the least share of Rs. 21.37 crores.

Scheme for Revenue Transfers :- The Commission's scheme for revenue transfer to states consist of:

- (i) tax shares in Income Tax and Union excise duties;
- (ii) sharing of additional duties of excise;
- (iii) the grant in lieu of the tax on railway passenger fares;
- (iv) financing of relief expenditure;
- (v) grants for upgradation and special problems;
- (vi) deficit grants; and
- (vii) grants for the plan revenue component.

Of the sharable taxes-income tax and Union excise duties-the recommendations of the Eighth Commission have been retained. It means 85 per cent of the proceeds of Income tax and 45 per cent of Union excise duties be given to the States, with 5 per cent in the latter being reserved for deficit States.

The sharing of additional excise duties in lieu of Sales Tax follows the formula of the Eighth Finance Commission.

The quantum of the grant in lieu of the railway passenger fare tax has been retained at the current level and is to be distributed according to the Eighth Commission formula.

The ninth Finance Commission submitted a unique report in the matter of grants. It suggested :

- (i) Grants for completing physical programmes (allowing for cost increases) envisaged by the Eighth Commission, i.e., the spill over into 1989-90

of the items covered in the 'previous award period of 1984-89.

- (ii) Grants to meet special problems of a non-plan character which comprise law and order problems in Punjab, Haryana, Himachal Pradesh and West Bengal (Rs. 135 crores), rehabilitation of Sri Lankan refugees in Tamil Nadu (Rs. 25 crores); and improvements in infrastructure in newly formed States of Arunachal Pradesh, Goa, Mizoram, Nagaland and Sikkim (Rs. 47 crores).
- (iii) Grants for development purposes which are logically in the nature of adhoc plan grants. These consist of grants 50 crores each for slum clearance in Bombay and Calcutta; grants amounting to Rs. 200 crores for the construction of school buildings, in 10 educationally backward States; and a grant of Rs. 10 crores for the development of the Dal Lake in Jammu & Kashmir.
- (iv) Indirect assistance has been extended to certain states by providing for a moratorium on interest and principal payments due in 1989-90. This relates to payments due on drought relief loans from eight states and on the special loans extended to Punjab in recent years.
- (v) The Commission also recommended the conversion of loans to Madhya Pradesh for the Bhopal gasleak tragedy into a long-term interest free loan adjustable against compensation to be obtained from Union Carbide.

Tenth Finance Commission :- The terms of reference of the Tenth Finance Commission are bound to become controversial inspite of the fact that the word "shall" does not appear in the guidelines. This time the controversial part of the terms of reference is "the objective of not only balancing the receipts and expenditure on revenue account of both the states and the Central Govt. but also generating surplus for capital investment and reducing fiscal deficit."

Another controversial aspect is the extension of the scope of Finance Commission's scrutiny from the earlier three public undertakings of the state Governments, namely irrigation projects, Electricity Boards and State transport undertakings, to all the developmental and commercial Public Sector enterprises. The concept of fiscal deficit is now, familiar to most economists and administrators. The need for its drastic reduction has been debated at the national level. Now, the terms of Reference of tenth Finance Commission have made it obligatory to achieve reduction of fiscal deficits at the State level also. This requirement may not be welcomed by the states. This is evident from the reaction of A. Das Gupta, Finance Minister of West Bengal, inspite of all this.

11th Finance Commission

Submitted its report on 2000, 7th July. A.M. Khusro was its Chairman. It accepted the already existing formula to recommend sharing of 28% of the shareable re-

sources with the states plus 1.5% on account of additional excise duties levied in lieu of sales tax. Increase was just 0.5 % which is very marginal.

Inter-state sharing formula adopted by the commission has led to wide spread resentment by the best performing states as it is more in the favour of poor performing states.

In order to maintain macro-economic stability and budgetary balances, it was required to review the financial position of Union and the states and to make suggestions for restructuring their financial position. It suggested that both centre and states were making unplanned expenditure which should be brought to the minimum i.e. strict financial discipline and generating more savings for investments. It also emphasised on overall growth and provision of basic services to all. Rs. 1860.72 cr. Under Upgradation and special Problem Grant has been released so far. Local Bodies grant Rs. 43, 46.66 crore released to the states.

After a careful analysis of the terms of references and recommendations, one gets an impression that the issues to be examined by the Finance Commission are pre-determined by the centre.

Eleventh Finance Commission : Other Recommendations

The Eleventh Finance Commission suggested (1) Institutional reforms regarding (i) federal fiscal reforms in order to reduce vertical imbalance and (ii) management and control of Debt and (II) Constitutional and legal changes mainly by (i) bringing services under the concurrent list and (ii) taking nominal limits for profession tax out of the constitution.

The other suggestions of the Eleventh Finance Commission emphasised the need for :

- widening the tax base by bringing services fully under tax net.
using profession tax and also taxation of farm incomes to augment tax revenue in states.
- ensuring better exploitation of the tax bases without increasing the tax rates.
- relying on user charges for enhancing non tax revenues.
- building up infrastructure in every state.
- cutting subsidies.
- transferring centrally sponsored schemes to the states along with funds.
- resizing the governments at all levels.
- improving public expenditure programme.
- introducing comprehensive structural reforms for public sector undertakings.
- restructuring financing of the special category states.

- strengthening the local bodies (Panchayats and municipalities) in the states.

Evaluation of Role :- All the Eleven Finance Commission set up so far, have made recommendations favouring the states in respect of their share, in income tax and the amount of grants-in-aid. The role of the Ninth Finance Commission in particular has been appreciated for recommending to states which are in need of assistance without linking them with the states being surplus or not. The Commission have in general liberalised the grant of relief to states affected by natural calamities like droughts, floods and cyclones.

Like a judge, the Finance Commission is working as an impartial body. According to B.N. Rao : “An innovation of far-reaching importance to the working of the Indian federal system is the Finance Commission, a quasi-arbitral body whose function is to do justice between the Centre and the States.”

The role of the Finance Commission is limited by a number of factors. It has to depend upon the State and information supplied by the states. Secondly, it has to work by accepting the revenue element of the plan as indicated by the Planning Commission for determining the quantum of devaluation and grants-in-aid to be made.

Twelfth Finance Commission was constituted with Dr. C. Rangarajan as Chairman, with three other members. The Commission submitted its report on November 30, 2004 covering the period 2005-10. TFC has

- enhanced the share of states in the net proceeds of the shareable central taxes to 30.5% from 29.5%.
- Raised the indicative limit of the revenue transfers to the states to 38 percent of the centre's gross revenue receipts from 37.5 percent recommended by the Eleventh Finance Commission.
- Change the formula for tax devolution with reallocation of weight in favour of population and efficiency factors and has dropped one of the factors (index of infrastrucutre) used by EFC.

In the end, we can conclude that in our constitutional set-up, the Finance Commission has far-reaching and enduring significance. Its importance can be seen from its position, functions and recommendations.

Table - 3
SHARE FOR THE STATES IN THE PROCEEDS
(INCOME TAX AND BASIC EXCISE DUTIES)

Finance Commission	Income Tax (%)	Basic Excise Duties (%)
First FC	55	40 of 3 duties
Second FC	60	25 of 8 duties
Third FC	66.7	20 of 35 duties
Fourth FC	75	20 of 45 duties

Finance Commission	Income Tax (%)	Basic Excise Duties (%)
Fifth FC	75	20 of 45 duties
Sixth FC	80	20 of 45 duties
Seventh FC	85	40 of all duties (larger relief to the poorer states)
Eighth FC	85	45 of all duties
Ninth FC	85	45 of all duties
Tenth FC	85	47.5 of all all duties
Eleventh FC	77.5	29.5 of all duties

Table-3 summarizes the recommendations of various Commissions, regarding sharing of taxes. Besides those recommendations, the Finance Commissions have also made recommendations about distribution of the proceeds of the Estate duty and the proceeds of the additional excise duties on tobacco, sugar and textiles to the States. The Commission also made recommendations about the grants in lieu of tax on railway passenger fares and about grants-in-aid to the States.

Major Recommendations of 13th Finance Commission

The Thirteenth Finance Commission (FC-XIII) was constituted by the President under Article 280 of the Constitution on 13 November 2007 to make recommendations for the period 2010-15. Dr. Vijay Kelkar was appointed the Chairman of the Commission. Dr. Indira Rajaraman, Professor Emeritus, National Institute of Public Finance & Policy (NIPFP), Dr. Abusaleh Shariff, Chief Economist, National Council of Applied Economic Research (NCAER), and Professor Atul Sarma, Former Vice-Chancellor, Rajiv Gandhi University (formerly Arunachal University) were appointed full time Members. Shri B.K. Chaturvedi, Member, Planning Commission was appointed as a part-time Member. Shri Sumit Bose was appointed as Secretary to the Commission. Subsequently, the President appointed Dr. Sanjiv Misra, Former Secretary (Expenditure), Ministry of Finance as Member of the Commission in place of Dr. Abusaleh Shariff, who was unable to join.

Main Recommendations

Finances of Union and States

1. The Ministry of Finance (MoF) should ensure that the finance accounts fully reflect the collections under cesses and surcharges as per the relevant heads, so that there are no inconsistencies between the amounts released to states in any year and the respective percentage shares in net central taxes recommended by the Finance Commission for that year. The states need to address the problem of losses in the power sector in a time-bound manner. Initiatives should be taken to reduce the number of Centrally Sponsored Schemes (CSS) and to restore the predominance of formula-based plan transfers.

Union Finances

2. The policy regarding use of proceeds from disinvestment needs to be liberalised to also include capital expenditure on critical infrastructure and the environment. Records of

landholdings of PSUs need to be properly maintained to ensure that this scarce resource is put to productive use, or made available for other public projects, or else, sold.

State Finances

3. The practice of diverting plan assistance to meet non-plan needs of special category states should be discontinued. With reference to public sector undertakings:

- i) All states should endeavour to ensure clearance of the accounts of all their Public Sector Undertakings (PSUs).
 - ii) The states should use the flexibility provided by the Comptroller and Auditor General (C&AG) to clear the backlog of PSU accounts.
 - iii) All states need to draw up a roadmap for closure of non-working PSUs by March 2011. Divestment and privatisation of PSUs should be considered and actively pursued.
 - iv) The Ministry of Corporate Affairs should closely monitor the compliance of state and central PSUs with their statutory obligations.
 - v) A task force may be constituted to design a suitable strategy for disinvestment/ privatisation and oversee the process. A Standing Committee on restructuring may be constituted under the chairmanship of the Chief Secretary to operationalise the recommendations of the task force. An independent technical secretariat may be set up to advise the finance departments in states on restructuring/disinvestment proposals.
4. With reference to the power sector: i) Reduction of Transmission and Distribution (T&D) losses should be attempted through metering, feeder separation, introduction of High Voltage Distribution Systems (HVDS), metering of distribution transformers and strict anti-theft measures. Distribution franchising and Electricity Services Company (ESCO)-based structures should be considered for efficiency improvement.
5. States with large cash balances should make efforts towards utilising these before resorting to fresh borrowings.

6. With reference to accounting reforms:

- i) The Government of India (GoI) should ensure uniformity in the budgetary classification code across all states. The list of appendices to the finance accounts of states also needs to be standardised.
- ii) Public expenditure through creation of funds outside the consolidated fund of the states needs to be discouraged. Expenditure through such funds and from civil deposits should be brought under the audit jurisdiction of the C&AG.
- iii) The following statements need to be provided with the finance accounts of states:
 - a) Comprehensive data on all subsidies.

- b) Consolidated information on the number of employees at each level, along with the commitment on salary. This statement should also include information on employees and their salary where such expenditure is shown as grants or booked under other expenditure.

Sharing of Union Tax Revenues

7. The share of states in net proceeds of shareable central taxes shall be 32 per cent in each of the financial years from 2010-11 to 2014-15. Under the Additional Duties of Excise (Goods of Special Importance) Act, 1957, all goods were exempted from payment of duty from 1 March 2006. Following this, the Centre had adjusted the basic duties of excise on sugar and tobacco products. In view of these developments, the states' share in the net proceeds of shareable central taxes shall remain unchanged at 32 per cent, even in the event of states levying sales tax (or Thirteenth Finance Commission Value Added Tax (VAT)) on these commodities. The Central Government should review the levy of cesses and surcharges with a view to reducing their share in its gross tax revenue. The indicative ceiling on overall transfers to states on the revenue account may be set at 39.5 per cent of gross revenue receipts of the Centre. The share of each state in the net proceeds of all shareable central taxes in each of the financial years from 2010-11 to 2014-15 shall be as specified in the following Table :

TABLE 1

States	Share of all Share of Shareable Taxes Excluding Service Tax(per cent)	Share of Service Tax (per cent)
Punjab	1.389	1.411
All States	100.000	100.000

Revised Roadmap for Fiscal Consolidation

8. The revenue deficit of the Centre needs to be progressively reduced and eliminated, followed by emergence of a revenue surplus by 2014-15. The following disclosures should be made along with the annual Central Budget/MTFP:

- i) Detailed breakup of grants to states under the overall category of non-plan and plan grants.
- ii) Statement on tax expenditure to be systematised and the methodology to be made explicit.
- iii) Compliance costs of major tax proposals to be reported.
- iv) Revenue Consequences of Capital Expenditure (RCCE) to be projected in MTFP.
- v) Fiscal impact of major policy changes to be incorporated in MTFP.
- vi) Public Private Partnership (PPP) liabilities to be reported along with MTFP.
- vii) MTFP to make explicit the values of parameters underlying projections for receipts and expenditure and the band within which they can vary while remaining consistent with targets.

9. Transfer of disinvestment receipts to the public account to be discontinued and all disinvestment receipts be maintained in the consolidated fund. GoI should list all public sector enterprises that yield a lower rate of return on assets than a norm to be decided by an expert committee. The FRBM Act needs to specify the nature of shocks that would require a relaxation of FRBM targets. In case of macroeconomic shocks, instead of relaxing the states' borrowing limits and letting them borrow more, the Centre should borrow and devolve the resources using the Finance Commission tax devolution formula for inter se distribution between states. Structural shocks such as arrears arising out of Pay Commission awards should be avoided by, in the case of arrears, making the pay award commence from the date on which it is accepted.

An independent review mechanism should be set-up by the Centre to evaluate its fiscal reform process. The independent review mechanism should evolve into a fiscal council with legislative backing over time. Given the exceptional circumstances of 2008-09 and 2009-10, the fiscal consolidation process of the states was disrupted. It is expected that states would be able to get back to their fiscal correction path by 2011-12, allowing for a year of adjustment in 2010-11.

- i) States that incurred zero revenue deficit or achieved revenue surplus in 2007-08 should eliminate revenue deficit by 2011-12 and maintain revenue balance or attain a surplus thereafter. Other states should eliminate revenue deficit by 2014-15.
- ii) The General Category States that attained a zero revenue deficit or a revenue surplus in 2007-08 should achieve a fiscal deficit of 3 per cent of Gross State Domestic Product (GSDP) by 2011-12 and maintain such thereafter. Other general category states need to achieve 3 per cent fiscal deficit by 2013-14.
- iii) All special category states with base fiscal deficit of less than 3 per cent of GSDP in 2007-08 could incur a fiscal deficit of 3 per cent in 2011-12 and Thirteenth Finance Commission maintain it thereafter. Manipur, Nagaland, Sikkim and Uttarakhand to reduce their fiscal deficit to 3 per cent of GSDP by 2013-14.
- iv) Jammu & Kashmir and Mizoram should limit their fiscal deficit to 3 per cent of GSDP by 2014-15.

10. States should amend/enact FRBM Acts to build in the fiscal reform path worked out. State-specific grants recommended for a state should be released upon compliance. Independent review/monitoring mechanism under the FRBM Acts should be set up by states. Borrowing limits for states to be worked out by MoF using the fiscal reform path, thus acting as an enforcement mechanism for fiscal correction by states. Loans from GoI to states and administered by ministries/departments other than MoF, outstanding as at the end of 2009-10, to be written off, subject to conditions prescribed. A window for borrowing from the Central Government needs to be available for fiscally weak states that are unable to raise loans from the market.

Local Bodies

11. Article 280 (3) (bb) & (c) of the Constitution should be amended such that the words 'on the basis of the recommendations of the Finance Commission of the State' are changed

to 'after taking into consideration the recommendations of the Finance Commission of the State'. Article 243(I) of the Constitution should be amended to include the phrase 'or earlier' after the words 'every fifth year'. The quantum of local body grants should be provided as per Table 10.4. The general basic grant as well as the special areas basic grant should be allocated amongst states as specified. The state-wise eligibility for these grants is placed in annexes 10.15a and 10.15c.

State Governments should appropriately strengthen their local fund audit departments through capacity building as well as personnel augmentation. The State Governments should incentivise revenue collection by local bodies through methods such as mandating some or all local taxes as obligatory at non-zero rates of levy, by deducting deemed own revenue collection from transfer entitlements of local bodies, or through a system of matching grants. To buttress the accounting system, the finance accounts should include a separate statement indicating head-wise details of actual expenditures under the same heads as used in the budget for both Panchayati Raj Institutions (PRIs) and Urban Local Bodies (ULBs). We recommend that these changes be brought into effect from 31 March 2012. The Government of India and the State Governments should issue executive instructions so that their respective departments pay appropriate service charges to local bodies. Given the increasing income of State Governments from royalties, they should share a portion of this income with those local bodies in whose jurisdiction such income arises. State Governments should ensure that the recommendations of State Finance Commissions (SFCs) are implemented without delay and that the Action Taken Report (ATR) is promptly placed before the legislature. Local bodies should consider implementing the identified best practices.

A portion of the grants provided by us to urban local bodies be used to revamp the fire services within their jurisdiction. Local Bodies should be associated with city planning functions wherever other development authorities are mandated this function. These authorities should also share their revenues with local bodies.

The development plans for civilian areas within the cantonment areas (excluding areas under the active control of the forces) should be brought before the district planning committees. State Governments should lay down guidelines for the constitution of nagar panchayats.

Disaster Relief

12. The National Calamity Contingency Fund (NCCF) should be merged into the National Disaster Response Fund (NDRF) and the Calamity Relief Fund (CRF) into the State Disaster Response Funds (SDRFs) of the respective states. Contribution to the SDRFs should be shared between the Centre and states in the ratio of 75:25 for general category states and 90:10 for special category states. The administrative mechanism for disaster relief to be as prescribed under the DM Act, i.e., the National Disaster Management Authority

(NDMA)/National Executive Council (NEC) at the Centre and the State Disaster Management Agency (SDMA)/State Executive Council (SEC) at the state level. Financial matters to be dealt with by the Ministry of Finance as per the existing practice. Prescribed accounting norms should be adhered to for the continuance of central assistance to the SDRFs.

Grants-in-aid to States

13. Total non-plan revenue grant of Rs. 51,800 crore is recommended over the award period for eight states. A performance grant of Rs. 1500 crore is recommended for three special category states who have graduated from a Non-plan Revenue Deficit (NPRD) situation.

Elementary Education

14. A grant of Rs. 24,068 crore is recommended for elementary education over the award period. The education grant will be an additionality to the normal expenditure of the states for elementary education. The expenditure (plan + non-plan) under elementary education, i.e., major head-2202, sub-major head-01, exclusive of grants recommended, should grow by at least 8 per cent annually during 2010-15.

Environment

15. An amount of Rs. 5000 crore is recommended as forest grant for the award period. Grants for the first two years are untied but priority should be given to the preparation of working plans. Release of grants for the last three years is linked to progress in the number of approved working plans. Twenty five per cent of the grants in the last three years are for preservation of forest wealth. These grants are over and above the non-plan revenue expenditure on forestry and wildlife (major head-2406) and shall be subject to the conditionalities. Seventy five per cent of the grants in the last three years can be used by states for development purposes. An amount of Rs. 5000 crore is recommended as water sector management grant for four years, i.e., 2011-12 to 2014-15 of the award period. Release of water sector grants would be subject to setting up of a Water Regulatory Authority and achieving the normatively assessed state-specific recovery of water charges.

Improving Outcomes

16. States should be incentivised to enroll such of their residents who participate in welfare schemes within the Unique Identification (UID) programme. A grant of Rs. 2989 crore is proposed to be given to State Governments in this regard. States should be incentivised to reduce their Infant Mortality Rates (IMR) based upon their performance beyond 31 December 2009. A grant of Rs 5000 crore is recommended for this purpose. A grant of Rs. 5000 crore is proposed to support improvement in a number of facets in the administration of justice. These include operation of morning/evening courts, promotion of Alternate Dispute Resolution (ADR) mechanisms, enhancing support to Lok Adalats, as

well as legal aid and training. A grant of Rs 20 crore is recommended for promotion of innovation by setting up a Centre for Innovation in Public Systems (CIPS) to identify, document and promote innovations in public services across states. The second grant of Rs. 1 crore per district is for the creation of a District Innovation Fund (DIF) aimed at increasing the efficiency of the capital assets already created.

Maintenance of Roads and Bridges

17. An amount of Rs. 19,930 crores has been recommended as grant for maintenance of roads and bridges for four years (2011-12 to 2014-15) of our award period.

State-specific Needs

18. A total grant of Rs. 27,945 crore is recommended for state-specific needs. In addition to the stipulations described in paras 5.52 and 9.82, state-specific grants are subject to the following conditionalities:

- i) No funds from any of the state-specific grants may be used for land acquisition by the states. Wherever land is required for a project/construction, such land may be made available by the State Government.

Monitoring

19. The High Level Monitoring Committee headed by the Chief Secretary to review the utilisation of grants and to take corrective measures, set up as per the recommendation of FC-XII, should continue.

20. The total grants-in-aid recommended for the states over the award period are :

Table 1.2: Grants-in-Aid to States

I Local Bodies Rs. 87519 crore

II Disaster Relief (including for capacity Building) Rs. 26373 crores

III Post-devolution Non-plan Revenue Deficit Rs 51800 crores

IV Performance Incentive Rs 1500 crores

V Elementary Education Rs 24068 crores

VI Environment Rs 15000 crores

(a) Protection of Forests Rs 5000 crores

(b) Renewable Energy Rs 5000 crores

(c) Water Sector Management Rs 5000 crores

VII Improving Outcomes Rs 14446 crores

(a) Reduction in Infant Mortality Rates Rs 5000 crores

(b) Improvement in Supply of Justice Rs 5000 crores

(c) Incentive for Issuing UIDs Rs 2989 crores

(d) District Innovation Fund Rs 616 crores

(e) Improvement of Statistical Systems at State and District Level Rs 616 crores

(f) Employee and Pension Data base Rs 225 crores

VIII Maintenance of Roads and Bridges Rs 19930 crores

IX State-specific Rs 27945 crores

X Implementation of model GST Rs 50000 crores

Total Rs 318581 crores

The Fourteenth Finance Commission (FFC)

The Fourteenth Finance Commission (FFC) was appointed on 2nd January, 2013 under the chairmanship of Dr. Y.V. Reddy. In addition to the primary objectives mentioned above, the terms of reference for the commission sought suggestions regarding the principles which would govern the quantum and distribution of grants-in-aid (non-plan grants to states), the measures, if needed, to augment State Government finance to supplement the resources of local Government and to review the State of the finances, deficit and debt conditions at different levels of Government.

Main Recommendations

The FFC has submitted its recommendations for the period 2015-16 to 2020-21. They are likely to have major implications for Centre-State relations, for budgeting and fiscal situation of the Centre and the States.

- The Fourteenth Finance Commission has radically enhanced the share of the States in the Central divisible pool from the current 32 percent to 42 percent which is the biggest ever increase in vertical tax devolution.
- The Fourteenth Finance Commission has also proposed a new horizontal formula for the distribution of the States' shares in the divisible pool among the States. There are changes both in the variables included/excluded as well as the weights assigned to them. Relative to the Thirteenth Finance Commission, the FFC has incorporated two new variables : 2011 population and forest cover and excluded the fiscal discipline variable.

Table-I

Horizontal Devolution Formula in the 13th and 14th Finance Commission

Variable	Weights Accorded	
	13 th	14 th
Population (1971)	25	17.5
Population (2011)	0	10
Fiscal Capacity/Income Distance	47.5	50
Area	10	15
Forest Cover	0	7.5
Fiscal Discipline	17.5	0
Total	100	100

Source : Reports of 13th and 14th finance commission

Tax Devolution

One of the core tasks of a Finance Commission as stipulated in Article 280 (3) (a) of the constitution is to make recommendations regarding the distribution between the union and States of the net proceeds to taxes. This is the most important task of any Finance Commission, as the share of States in the net proceeds of union taxes is the predominant channel of resource transfer from the Centre to States.

Divisible Pool

The divisible pool is that portion of gross tax revenue which is distributed between the Centre and the States. The divisible pool consists of all taxes, except surcharges and cess levied for specific purpose, net of collection charges.

Prior to the enactment of the Constitution (Eightieth Amendment) Act, 2000, the sharing of the union tax revenues with the states was in accordance with the provisions of articles 270 and 272, as they stood then. The eightieth amendment of the constitution altered the pattern of sharing of union taxes in a fundamental way. Under this amendment, article 272 was dropped and article 270 was substantially changed. The new article 270 provides for sharing of all the taxes and duties referred to in the union list, except the taxes and duties referred to in articles 268 and 269, respectively, and surcharges on taxes and duties referred to in article 271 and any cess levied for specific purposes.

Grants-in-aid

Horizontal imbalances are addressed by the Finance Commission through the system of tax devolution and grants-in-aid, the former instrument used more predominantly. Under Article 275 of the constitution, finance commissions are mandated to recommend the principles as well as the quantum of grants of those States which are in need of assistance and that different sums may be fixed for different States. Thus one of the pre-requisites for grants is the assessment of the needs of the States.

The First Commission had laid down five broad principles for determining the eligibility of a State for grants. The first was that the budget of a State was the starting point for examination of a need. The second was the efforts made by States to realize the potential and the third was that the grants should help in equalizing the standards of basic services across States. Fourthly, any special burden or obligations of national concern, though within the State's sphere, should also be taken into account. Fifthly, grants might be given to further any beneficent service of national interest to less advanced States.

Grants recommended by the Finance Commissions are predominantly in the nature of general purpose grants meeting the difference between the assessed expenditure on the non-plan revenue account of each State and the projected revenue including the share of a State in Central taxes. These are often referred to as 'gap filling grants'. Over the years, the scope of grants to States was extended further to cover special problems. Following the seventy-third and seventy-fourth amendments to the Constitution, Finance Commissions were charged with

the additional responsibility of recommending measures to augment the Consolidated Fund of a State to supplement the resources of local bodies. This has resulted in further expansion in the scope of Finance Commission grants. The Tenth Commission was the first commission to have recommended grants for rural and urban local bodies. Thus, over the years, there has been considerable extension in the scope of grants-in-aid.

Fiscal Capacity/Income Distance

The income distance criterion was first used by Twelfth FC, measured by per capita GSDP as a proxy for the distance between states in tax capacity. When so proxied, the procedure implicitly applies a single average tax-to-GSDP ratio to determine fiscal capacity distance between states. The Thirteenth FC changed the formula slightly and recommended the use of separate averages for measuring tax capacity, one for general category states (GCS) and another for special category states (SCS).

Fiscal Discipline

Fiscal discipline as a criterion for tax devolution was used by Eleventh and Twelfth FC to provide an incentive to States managing their finances prudently. The criterion was continued in the Thirteenth FC as well without any change. The index of fiscal discipline is arrived at by comparing improvements in the ratio of own revenue receipts of a State to its total revenue expenditure relative to the corresponding average across all States.

- Several transfers have been proposed including grants to rural and urban local bodies, a performance grant along with grants for disaster relief and revenue deficit. These transfers total to approximately 5.3 lakh crore for the period 2015-20.
- The FFC has not made any recommendation concerning sector specific grants unlike the Thirteenth Finance Commission.
- An allocation of 5600 crore has been required for maintenance for rural roads Pradhan Mantri Gram Sadak Yojana and Mukhya Mantri Gram Sadak Yojana.
- The FFC recommendations are expected to add substantial spending capacity to States' budgets. The additional spending capacity can better be measure by scaling the benefits either by NSDP at current market price or by States' own tax revenue. In terms of the impact based on NSDP, the benefits of FFC transfers are highest for chhattisgarh, Bihar and Jharkhand among the GCS and for States like Arunachal Pradesh, Mizoram and Jammu & Kashmir among the SCS while in terms of States' own tax revenues, the largest gains accrue to GCS of Bihar, Jharkhand and Chhattisgarh and SCS of Arunachal Pradesh, Mizoram and Nagaland.

Some caveats or complications to this exercise must be noted. First, they are sensitive to the assumptions underlying GDP growth, revenue and expenditure estimations/projections for 2014-15 and 2015-16. Secondly, assumptions are also made about CAS amounts in 2014-15 and about reductions in CAS amounts in 2015-16. So, these must be treated as illustrative calculations. For example, another option would simply be to transfer those schemes that are

on State list back to the States. Also, estimates have only been presented for the year 2015-16. Thereafter, additional factors such as GST implementation and the next Pay Commission awards will affect projections beyond the coming year.

With these caveats, The FFC has made far-reaching changes in tax devolution that will move the country toward greater fiscal federalism, conferring more fiscal autonomy on the States. This will be enhanced by the FFC-induced imperative of having to reduce the scale of other central transfers to the States. In other words, States will now have greater autonomy on the revenue and expenditure fronts. The numbers also suggest that this renewed impulse toward fiscal federalism need not be to the detriment of the center's fiscal capacity. A collateral benefit of moving from CAS to FFC transfers is that overall progressivity will improve.

To be sure, there will be transitional costs entailed by the reduction in CAS transfers. But the scope for dislocation has been minimized because the extra FFC resources will flow precisely to the States that have the largest CAS-financed schemes.

In sum, the far-reaching recommendations of the FFC, along with the creation of the NITI Aayog, will further the Government's vision of cooperative and competitive federalism. The necessary, indeed vital, encompassing of cities and other local bodies within the embrace of cooperative and competitive federalism is the next policy challenge.

Conclusion :- The Finance Commission is a remarkable example of Union-State co-ordination and co-operation that finds no parallel in any other system of the world. "The Chief merit of the work of the Commission lies in its impartial and objective outlook as a steadying force in the finances of the federal system and its ability to take the question of distribution of finance out of the vortex of federal state political pressures and controversies. In fact, the Commission acts as a buffer between the Union and the States, checking the clamorous finance-hungry States bent upon applying their political pressure on the Union. and the States, making the latter as much as possible to the needy states. It will be almost impossible for the Union to go against the recommendations of the Commission." The role of the Finance Commission, in actual practice, has been overshadowed by the role of Planning Commission, an extra-constitutional agency. It has been reduced to the status of an ancillary wing of the Planning Commission. The Finance Commission is virtually directed to submit its recommendations in a way at a time so as to facilitate the working of the Planning Commission.

In brief, we may agree that transfers through the Finance Commission which is a statutory body contributed only about 1/3 of total transfers from the centre to the states. This means that about 2/3 of the transfers are channelled through the planning commission or the central Govt. directly, since the centre contributed a large amount of resources in the form of discretionary grants to the states, it required considerable powers to effect the decision-making processes at the State level. This led to further erosion of autonomy of the states.

LESSON NO. 2.4

PARLIAMENTARY CONTROL OVER FINANCE

In the words of the famous philosopher W.E. Gladstone, 'The Finance of the country is ultimately associated with the Liberties of the country. This is particularly true of England and the pure democratic countries of the West, where the power of the purse has been a powerful method of legislative control over the Executive in India. Actually, the evolution of Legislative Control was closely linked with the struggle for freedom from foreign rule. Consequently, Legislative Control did not develop any teeth before national independence. In England, the control Principle behind legislative control was that, the crown demands money, the common grant and the lords assent to the grant. "but in India under the British crown taxes were levied without the consent of the Indian people and their elected representatives. As for expenditure before 1921, powers of legislature were limited to discussion and criticisms. But the executive was free to accept or reject. But during 1921-1937 the legislature voted the votable grants, the legislative committee could examine the estimates and the accounts, but the Governor General could restore any cut and sanction expenditure disallowed by the Legislature if he was satisfied that the amount was essential to discharge of his responsibilities to ensure, the safety and tranquility of exercise. In British India the Secretary of state a member of British Cabinet continued to exercise the ultimate authority over Indian Affairs.

In brief, 'the accountability of the executive to the legislature is the basic principle and the most important feature of parliamentary form of Government. It is the duty of the legislature to scrutinise and control government activities and satisfy itself that policies-pursued by the government are aimed at satisfying the needs and aspirations of the people. And, the best method of realising this control is exercised through the instrument of finance. The Constitution of India enjoins through Article 113 (3) that "No. demands of grant shall be made except on the recommendation of the President." And, to ensure supremacy of Parliament, Article 256 states: "No tax shall be levied or collected except by authority of law." Appropriation of money is done by Parliament or the State legislature as the case may be. Further, Article 256 (3) states: "No money out of the 'Consolidated Fund of India or the Consolidated Fund of State shall be appropriated except in accordance with law and in the manner provided in this Constitution."

Legislative Control Over Finance :- The legislative control over finance may appropriately be compared to that of the shareholders of a company upon the Directors.

The legislative control over finance in India can be discussed at two stages:

1. Control before the money is actually appropriated; and
2. Control after the money is appropriated.

1. Control before Appropriation :- Before the money is finally sanctioned by Parliament, it exercises control through various devices such as :

(i) Budgetary Discussion :- The functioning of each and every department of the government comes under close scrutiny at the time the demands of that department as provided in the budget come under discussion of the legislature. It is a time when every kind of question can be raised regarding the functioning of the department concerned. Questions of policy, economy, grievances, complaints etc. are usually raised and the minister concerned has to give a satisfactory reply.

It is, however, a few days after the Budget has been presented to the House that general discussion takes place on it. The Budget is presented to the Lok Sabha usually at 5 p.m. on the last day of February by the Finance Minister with a Budget speech. There is no discussion on that day.

At the time of general discussion, “the House shall be at liberty to discuss the Budget as a whole or any question of principle involved therein, but no motion shall be moved nor shall the Budget be submitted to the vote of the House.”

(ii) Voting of Demands :- When the general discussion of the Budget is over, the Lok Sabha proceeds to voting of Demands for Grants, that is voting of the expenditure part of the Budget. The demand is made in a motion, “that a sum not exceeding Rs. ‘X’ be granted to the President to defray the charge which will come for payment during the year ending 31st March, 20..... in respect of (the subject of) Demands “A demand, when voted, becomes a grant.

(iii) Cut-Motions :- To these demands three kinds of Cut-Motions can be moved to reduce the amount of a demand in any of the following ways:

(a) Policy Cut Motion :- In order to show disapproval of the policy underlying the demand, it is proposed “That amount of the demand be reduced to Rs. 1/- The member giving notice of such a motion shall indicate in precise terms, the particulars of the policy, which he proposes to discuss. The discussion shall be confined to the specific point or points mentioned in the notice it shall be open to members to advocate an alternative policy.

(b) Token Cut :- This type of motion is in the form the “amount of the demand be reduced to Rs. 100/-. It is proposed with a view to ventilate a specific grievance and discussion shall be confined to that particular grievance.

(c) Economy Cut :- Such a motion is meant to reduce the demand by a specific amount which the members feel as unnecessary and wasteful. The amount actually represents the economy that can be effected. Such specified amount may be either a lump-sum reduction in demands or omission or reduction of an item in the demand.

The notice shall indicate briefly and precisely the particular matter on which discussion is sought to be raised and speeches shall be confined to the discussion as to how economy can be effected.

It is on the basis of Cut Motions that discussion on the demands starts in Parliament. It must, however, be remembered that the members cannot make any addition to or increase in any item of expenditure proposed in the Budget. They can only reject or reduce the amount of expenditure. In the Indian Parliament, only Token Cut Motions are moved.

As demands of each Ministry are taken up, the Speaker puts the Demands and Cut Motions together before the House for discussion. At the end of the discussion, the Minister incharge of the Department makes a reply to the discussion, in which he replies to the criticism and also gives assurance for the removal of the grievances pointed out to the members. At the end of the reply of the Minister, either the Cut Motions are withdrawn, or they are put to vote. In the voting, the Cut Motions are rejected because the Cabinet has a majority in the House.

(d) Appropriation Bill: Appropriation Bill provides second opportunity to the Parliament to consider the demands. The Appropriation Bill gives legal effect to the demands as voted by the House, and authorises the issue of money for those purpose from the Consolidated Fund of India. Its passage follows the same procedure in the Lok Sabha as any other Bill except that no amendments can be moved to the grant as voted by the House or to the Consolidated Fund charges,. "The debate on an Appropriation Bill shall be restricted to matters of public importance or administrative policy implied in the grants covered in the Bill which have not already been raised while the relevant demands for grants were under consideration."

The Rajya Sabha to which the Bill is then sent, has no power to reject or amend the Bill. It can only discuss the Bill and make recommendations within 14 days to the Lok Sabha, which may accept or reject them. In either case, the Appropriation Bill will be sent to the President for his assent after 14 days of its passage in the Lok Sabha. The President cannot return a Money Bill for consideration.

(e) Supplementary Grants :- It is a general rule that the amount sanctioned by the Parliament for a particular purpose would be spent only for that purpose. It may happen that the amount already sanctioned may fall short. It is the inadequacy of funds for a particular purpose that necessitates supplementary grants. Here also the executive has to present every item of expenditure and their objective before Parliament.

(f) Excess Grants :- It may be that money spent on any service during a financial year is in excess of the amount sanctioned for that service and for that year. In such case, Excess Grant is introduced in the House to regularise the excess amount spent over and above the original grant approved by Parliament.

(g) Vote on Account :- The financial year in India begins from April. It may

be that the Parliament is not able to complete budget discussion before the beginning of the new financial year or due to any other cause. In such a case, the Lok Sabha has the power to pass vote on account providing the Government with the authority to draw funds. This is what happened during the financial year 1991-92 when vote on account was passed till July 1991 when the Chandrashekhar Government was in power.

(h) Vote of Credit :- Article 116 (1) 'b' of Constitution enables the House to make a grant for meeting an unexpected demand upon the resources of India when an account of the magnitude or the indefinite character of the services, the demand cannot be stated with the details ordinarily given in the Annual Financial Statement.

(i) Reappropriation:- It means appropriating an amount to another head from the original head for which it was sanctioned. It happens when expenditure on some head falls short of the grant while in another it shoots up. It is thus simply an adjustment of the grant already made. Reappropriation therefore, can be made from a minor head to another minor head.

(j) Parliamentary Questions :- In addition to budgetary debates, there are various other ways in which financial matters can be raised and discussed in Parliament. It is that first hour of every day's discussion (except once a week) is devoted to questions and answers. During this hour also financial questions can be raised.

2. Control After Appropriation :- The second stage of legislative control over finance starts after the budget has been passed. It has to see that the executive spends money only for the purpose for which it was sanctioned. This control is exercised through getting the accounts audited by an independent constitutional authority, 'the Comptroller and Auditor General of India. Besides, control is also exercised through legislative committees constituted for the purpose.

(i) Audit Reports :- "Audit, like the judiciary, the executive and the legislature, is one of the important ingredients of democracy." Audit is conducted by an Independent constitutional authority Known as the Comptroller and Auditor General of India. Under him are one Accountant General at the State level and one Accountant General Central Revenues for auditing accounts of the States and Union respectively. They all submit the annual statements of audit based on a particular financial year, pointing out financial irregularities and lapses on the part of various departments, if any. This report is presented by the Public Accounts Committee which has on it members of almost all political parties. It is then through the Finance Department of the State concerned and the Ministry of Finance in the case of the Union Government that necessary replies are sent to the respective Accountant General.

(ii) Control Through Committees :- Parliament or the State Legislature, what ever the cases may be, is not in itself in a position, because of unwieldy size to keep a close scrutiny on the accounts and operations of various departments.

For this purpose, their various committees of Parliament such as Public Accounts Committee, Estimates Committee and Committee on Public undertakings in every State Legislature. The function of the first two committees which are considered as 'two eyes' of the legislature is to control taxation, to vote supplies for expenditure and to ensure that the executive utilises the funds only for the purpose they were sanctioned. The third committee exercises functions in relation to Public Undertakings while the first two in respect of governmental department. The function of Estimates Committee is to effect economy in administration through suggestions as to what economies and improvements in organisation can be made to secure efficiency. It can also suggest alternative policies.

Conclusion: In this way, we find that not only is the passage of budget necessary but also that proper control should be maintained by the legislature over the executive which utilises it for performing the public policies laid down. Money is such an element which needs proper control for its utilisation otherwise irregularities are bound to occur here and there. It is with this relations that the legislature exercise control over the executive while passing the budget and even after it has been passed and being executed.

SUGGESTED BOOKS

1. Fiscal Federalism in India : R.K.Sinha
2. Finance Commissions and
Centre-State Relations in India : S.S. Januja
3. Centre-State Financial Relations
and Finance Commission in India : Ph. D. Thesis by S.S. Januja
4. Financial Administration : Thavaraj

SELF -CHECK EXERCISE

1. The Parliament under certain conditions can frame laws on state list.
2. The Indian constitution vests the residuary powers in the States.
3. Income Tax falls in the state list.
4. Sources of income for states are very meager.
5. Union Government helps the states by giving financial aid.
6. Recommendations of a Financial Commission are obligatory.
7. In Financial Emergency the State Money Bills are reserved for consideration of President.
8. The state have to comply with the direction given by the Union Government.

PARLIAMENTARY FINANCIAL COMMITTEES

In India, the evolution of legislative financial control was closely linked with the Struggle for freedom from foreign rule. Consequently, legislative control did not develop any teeth before national independence, (i.e. from 1858-1947), taxes were levied without the consent of the Indian people and their elected representatives. As far as possible, expenditure, before 1921, powers of legislature were limited to discussion and criticisms. But the executive was free to accept or reject. But during 1921-1947, the legislature voted the votable grants, the legislative committee could restore any cut and sanction expenditure disallowed by the legislature if he was satisfied that the amount was essential to discharge of his responsibilities to ensure the safety and tranquility of British Indian Secretary of the State, a member of the British Cabinet, continued to exercise the ultimate authority over Indian affairs. In the words of W.E.Gladstone, the finance of the country is ultimately associated with the liberties of the country. This is particularly true of England and the democratic countries of the West, where the power over the purse has been a powerful tool of legislative control over the executive.

Legislative Approval of the Budget

The Constitution of India provides that:

“The President shall in respect of every financial year cause to be laid before both the Houses of Parliament a statement of the estimated receipts and expenditure for the government of India for that year.”

How the budget is prepared and discussed in the legislature is already discussed in the one of the lessons. The budget goes through the following stages before it is passed finally. by the Parliament or state legislature as the case may be :

1. Presentation to the legislature;
2. General discussion
3. Discussion and voting of Demands for Grants;
4. Consideration and passing of Appropriation Bill; and
5. Consideration and passing of the Finance Bill;

In the Central Government, the discussion on the financial estimates lasts for about two months. During the budget session, the legislature gets an opportunity to discuss the fiscal policies of the government before approving the financial estimates.

Authorising the expenditure proposals and tax measures is only the first phase of legislative control. The legislature is equally concerned that the expenditure authorised

is incurred for the purposes that were intended. It is also interested about efficient and economical utilisation of funds. The legislative is assisted by the Comptroller and Auditor General of India and his outfit in its quest for legality and regularity of expenditure. The auditor is also expected to probe into the propriety of transactions and performance of agencies. The audit is conducted on the basis of the detailed accounts of the actual expenditures incurred and revenues collected. Until recently auditing and accounting were combined in the same agency. But since 1976 accounts are separated from audit at the centre. Some state governments have also separated the audit from accounts. The auditors report forms the basis of legislative control after budget is implemented. Besides, the legislature interests itself about the policies and organised implications or public expenditure having a bearing on efficiency and economy.

It would have been cumbersome if the entire house was to examine the audit report or conduct enquiries about the policy of organisation, implications of expenditure. Hence, the experience in all parliamentary government is that the House constitutes select committees to examine the estimates of expenditure reports. Since independence up to 1964, there were only two major financial committees of parliament viz. Estimates Committee and the Public Accounts Committee. But since 1964, a separate committee called "The Committee on Public Undertakings" was constituted to examine the estimates and scrutinise the accounts relating to the commercial activities of the public sector. State legislatures also having similar committees though all of them do not have separate committees on public undertakings.

I. Estimates Committee

The Estimates Committee came into being in 1950. Its predecessor was the Standing Finance Committee, which was constituted in 1921. This committee depended on the will of the executive. It has no statutory status. Its functions were not clearly defined and its deliberations were not satisfying to the elected representative of the Legislative Assembly.

Composition

The Estimates Committee constituted since 1950 had 25 members. From 1956 the membership was raised to 30. It is select committee elected by the members of the Lok Sabha from amongst themselves according to the convention, two-thirds of the members are re-elected for another year. The term or office of members is one year. The Chairman of the Committee is nominated by the Speaker from amongst the members of the committee. If the Deputy Speaker is a member of the committee, he is appointed its chairman, otherwise a senior member of the ruling party is nominated.

Functions

The Committee examines such of the estimates which it may deem fit or are specifically referred to it by the Lok Sabha or the speaker with a view to:

- (a) report what economic improvements in organisation, efficiency or administrative reform consistent with the policy underlying the estimates

may be affected;

- (b) suggest alternative policies in order to bring about efficiency and economy in administration;
- (c) examine whether the money is well laid out within the limits of the policy implied in the estimates; and
- (d) suggest the form in which the estimates shall be presented to Parliament.

While examining the policies of the government, the Estimates Committee is not to lay down any policies. They could see whether the policies laid down by the parliament are carried out. Being a financial committee, it is concerned with all matters in which finances are involved. Because the way policies are implemented will be reflected in the expenditure incurred. The basic functions of the committee is to ensure efficiency and economy in administration. If waste is noticed it can suggest change in the policy for the considerations of the House.

The Estimate Committee can constitute one or more sub committees. The report of the sub-committees are deemed as report of the whole committee.

Method of Working

Once a decision is taken as to the estimates to be examined the committee collects material required for an adequate examination of the expenditure. It interviews officials, issues questionnaire to the concern Ministry Departments, calls Witnesses for proper records and files and so on. If the disclosure of any document is not in public interest the, matter is referred to the speaker for his guidance. The committee submits its reports to the House. The draft report is shown to the speaker before finalisation.

The recommendations of the Estimates Committee relate to. :

- (a) improving the organisation and working of the department;
- (b) affecting economy; and
- (c) general aspects

Functional and Economic classifications of budget; introductions of performance budgeting and so on are some of the far reaching recommendations of the committee.

II. Public Accounts committee

Historically, the Webby Commission 1896 indicated the need for an Accounts committee to highlight financial irregularities. The Montagu Chelmsford Reform suggested the creation of such committees out of the provincial legislature. The first committee on Public Accounts at the centre to deal with the Appropriations Accounts of Governor General in council and the report of the Auditor General then Public accounts committee at the provincial level were also meant to examine whether money voted has been duly spent within the prescribed scope and purpose.

Assisted by the Auditor General

These committees were assisted by the Auditor General of India who was given

statutory recognition under the Government of India Act of 1919. Auditor General was intendant of the government so as to enable him to perform his watch dog function effectively. He was the intelligent officer of the public Accounts Committees.

In fact, the scope and functions of audit were broad. The Auditor General performed two major functions, namely, that of keeping the accounts of the government and audit them. Accounts were too complex. He had to simplify them with a view to make them intelligible to the legislature and its committees. Accuracy, completeness and consistency of classification were some of his important concerns. Besides he had to go through these accounts with a fine toothed comb. Secondly he had to be vigilant about illegalities, irregularities, extravagance and waste.

As far as the expenditure is concerned, the Indian financial system is built upon sanctions. The audit scrutinises these sanctions to see not only whether they are within the rules or within the power of sanctioning authority but also whether they fall within the proper cannons of finance. The reports of Auditor General constituted the principal source of information for the investigators of the public accounts committees.

Before Independence, the membership of the Public Accounts Committee in the Centre ranged between 12 and 20. Half of them were elected every year based on proportional representations by means of single transferable vote. The Governor General used to nominate four of them. The Finance Member of the Viceroy's executive was the chairman of the committee.

The Committee was:

- (a) to ensure proper record of fiscal transactions of government,
- (b) to ensure legislative control over the financial activities of the executive;
- (c) to check waste and extravagance.

Apart from irregular, illegal and wasteful expenditure the committee was concerned about indiscriminate reappropriations especially from grant to grant or from voted to non voted, supplementary grants and expenditure. Its attention was also focused on 'New Services' / Military accounts were outside its purview upto 1931 since when Military Accounts Committee was constituted. The Finance Member being the Chairman of the Committee, to some extent, inhibited its deliberations. Nevertheless the reports of the Committee were discussed by the Assembly and the Finance Department took steps to implement recommendations of the Committee.

The Public Accounts Committee since Independence

Under the provisions of the Constitution, the Public Accounts Committee at the Centre is constituted by both the houses of the Parliament and is composed of 22 members, 15 from the Lok Sabha and 7 from the Rajya Sabha. The members are elected through a system of proportional representation by a single transferable vote. Almost every sizeable party or group is represented in the committee. Although the committee is elected annually, there is a convention that there should be a two year tenure of the membership to ensure continuity. The Chairman of the committee is nominated

by the Speaker from amongst the members of the committee. Until 1966-67, the chairman belonged to the ruling party. Since then a member by the opposition has been named the Chairman.

Function of the Committee

The functions of the committee are to examine the accounts showing the appropriation of sums granted by the Parliament for the expenditure of the government, the annual finance accounts of the government and such other accounts laid before the house, as the committee may deem fit. While scrutinising the Appropriation Accounts and the Audit Report thereon by the Comptroller and Auditor General, the Public Accounts Committee has to satisfy itself that;

- (a) due economy has been exercised in the financial transactions of the executive government; and
 - (b) public moneys have been spent by the executive government as the parliament intended it to be spent;
 - (c) high standards of public morality have been observed in all matters of finance.
- While doing so it is the duty of Public Accounts Committee to satisfy itself, that
- (i) money shown in the accounts as having been disbursed were legally available for and applicable to, the service or purpose to which they have been applied or charged.
 - (ii) the expenditure conforms to the authority which governs it ; and
 - (iii) every reappropriation has been made in accordance with the provisions made in this behalf under rules framed by competent authority.

It shall also be the duty of the Public Accounts Committee:

(a) to examine in the light of the report of the Comptroller and Auditor General, the statement of accounts showing the income and expenditure of the state corporations, manufacturing schemes, concerns and projects together with the balance sheets and statement of profit and loss accounts which the President may have required to be prepared or are prepared under the provisions of the statutory rules regulating the financing of a particular corporation, trading or manufacturing scheme or concern or project and the report of the Comptroller and Auditor General there on excepting such public undertakings as have been allotted to the committee on the public Undertakings:

(b) to examine the statement of accounts showing the income and expenditure of autonomous and semi autonomous bodies, the audit of which may be conducted by Comptroller and Auditor General of India, either under the directions of the President or by a Statute of Parliament; and

(c) to consider the report of the Comptroller and Auditor General in cases where the President may have required him to conduct an audit to any receipts or to examine the accounts of stores and stocks.

The Committee is also to examine money spent on any service during a

financial year in excess of the amount granted by the Parliament for that purpose. While investigating such an excess the Committee goes into the facts of each case and circumstances leading to it.

Working of the Committee

The Public Accounts Committee can organise itself into sub-committees and working groups. When approved by the Committee, the reports or the sub-committees are deemed to be the reports of the Public Accounts Committee.

The Committee can call for appears, persons, records etc. to facilitate its investigation. Usually, Heads of Departments responsible for expenditure appear before Committee to answer any questions or criticisms which it might like to ask or make. Only in exceptional cases, has the concerned Minister appeared before the committee.

The Committee is assisted in its work by the Comptroller and Auditor General who is the 'acting hand' the guide, philosopher and friend of the Committee. The CAG is not a member of the committee. He attends the meetings on invitation. Normally he does not ask question. But, whenever necessary, he can, with the permission of the chairman, ask a witness to clarify a particular point relevant for the issue in questions. As a right hand man of the Chairman, he acquaints him with the technicalities of the matters dealt with.

Apart from calling witness, the committee can call of memoranda from private investigations and examination of witness and other sources of information, the committee reaches final conclusions. The chairman submits the reports of the committee to the Parliament in the instalment as and when they are ready. A summary of the minutes of the proceedings of the committee is also included as a part of the report. But the evidence is not published. The report is treated 'Secret' till it is presented to the House of Parliament.

Though the Parliament can, it seldom discusses these reports. The committee insists on the ministry/undertaking concerned to inform them about the implementation of recommendations made by them in the reports. The committee reviews the replies and along with its comments planted and presented to both the Houses of Parliament.

The Control exercised by PAC is quite significant, as it is considered to control financial matters. The nature of control is quasi-judicial, it is done by an expert body. As a watchdog activity performed by all-committee acts as deterrent on excesses committed by the executive.

Committee on Public Undertakings

Planned economic development has led to an unprecedented growth of public sector embracing commercial and industrial enterprises in India. Parliament has vested enormous funds out of the consolidated Fund of India. Parliament is, therefore, concerned about the proper utilisation of these funds. until 1964, the Public Accounts Committee and the Estimate Committee exercises the requisite control. But on the

recommendation of the Krishan Menon Committee a separate Committee called the Committee on Public Undertakings was constituted for this purpose on May 1, 1964.

At present, the Parliament exercises control through a number of ways :

- (a) through questions in Parliament;
- (b) through debates in the House and discussion on demands for grants for the Ministry/Department concerned;
- (c) through discussions on the annual reports of the undertaking; and
- (d) through examination by the Committee on Public Undertakings.

Earlier the Committee consisted of upto 10 members elected by the Lok Sabha from amongst its members according to the principle of proportional representation by means of a single transferable vote. Five members from the Rajys Sabha, elected similarly, are associated with the Committee. The Chairman of the committee is nominated by the Speaker from amongst the members of the Lok Sabha. **Now it has 15 members of Lok Sabha and 7 members of Rajya Sabha.**

Functions of the Committee

The functions of the Committees on public undertakings are :

- (a) to examine the reports and accounts of such public undertakings as have been specifically allocated to the committee for the purposes;
- (b) to examine the report, if any of the Comptroller and Auditor General on Public Undertakings;
- (c) to examine in the context of the autonomy and efficiency of public undertakings, whether the affairs of the public undertakings are being managed in accordance with sound business principles and prudent commercial practices; and
- (d) to exercise such other functions vested in the Public Accounts Committee and the Estimate Committee in relations of the Public undertakings specified for the committee as are not covered by clauses (a), (b) and (c) above and as may be allotted to the Committee by the Speaker from time to time.

The Committee shall examine and investigate any of the following matters :

- (i) matters of major government policy, business or commercial functions of the public undertakings;
- (ii) matters of day- to-day administration; and
- (iii) matters for the consideration of which machinery is established by a special statute under which a particular undertaking is established.

The examination of public undertakings by the Committee on Public Undertakings is, therefore, in the nature of evaluations by, the performance of public undertaking, covering important aspects such as implementations of policies, programmes, management, financial success etc.

Working of the Committee:

In the beginning of the year, the committee decides upon the subjects or the undertakings proposed to be examined during the year. The examinations of the committee may be comprehensive or limited to the working of an undertaking which is considered to be of topical interest. The chairman of the committee is authorised to ascertain full details information from the undertaking concerned without prior reference to the committee.

The source of information utilised by the committee may be as follow :

- (a) preliminary and detailed information submitted by the Ministry / Department or Undertaking concerned with the subjects to be examined;
- (b) Memoranda on the subjects under study submitted by non official organisations such as Chambers of Commerce, trade organisation, professional consultants, trade - unions etc.
- (c) evidence given by officers or the undertaking, Ministry / Department and
- (d) audit reports (commercial) and the 'Memorandum of Important points submitted by the Comptroller and Auditor General.

The draft report of the committee is sent to the undertaking ministry / Department, Ministry of Finance as well as the CAG for actual verification. The report is finalised on the basis of the factual information received from these agencies. The final report is submitted to the parliament. Naturally, such well considered reports containing a mass of useful information and factual data are highly appreciated. Some of the cases the board studies relating to the townships and factory building of public undertakings, financial management and so on are also founded extremely useful and informative.

As a matter of convention the reports of the CPU as in the case those PAC and EC are not discussed in the House. But the action taken on the report is elicited from the concerned undertaking, Ministry Department etc. are gathered and a consolidated action taken. Report is prepared and submitted by the Committee to the Parliament.

The control exercised by the CPU is somewhat limited. Firstly, there are about 13 public undertakings. Of this hardly ten undertakings are examined by the committee every year. It follows that the CPU can examine each undertaking only once every ten years or so. Secondly, the examination of the committee is such that it does not normally drive into technical matters. The members of the committee do not have the necessary expertise and background for deeper study and analysis.

Broadly speaking, in modern government legislative financial control has become more nominal than real. Under the Cabinet systems, when the budget is discussed on the floor of the House, very seldom we come across a cut in estimates of expenditure though there is an armory full of such provision. With regards to revenues, the concessions conceded are more symbolic than substantial. The Estimates Committee deals more with economy and efficiency through administrative

reforms and reorganisation of various departments in view than with a direct reduction in expenditure. The PAC basis its deliberations on a post mortem report produced by the audit, sometimes relating to some distant past rather than with matters. which could create an impact on the current financial performance in the end, it is check rather than effective control. 17 Department Related Standing Committees were set up on 8 April, 1993. The functions of these committees are :

- (a) to consider the Demands for Grants of various ministries / Departments of Government of India and make reports to the Houses.
- (b) To examine such Bills as are referred to the Committee by the Chairman, Rajya Sabha or the Speaker, Lok Sabha as the case may be and make reports there on.
- (c) To consider Annual Reports of Ministries/Departments and make reports thereon
- (d) To consider policy documents presented to the Houses, if referred to the Committee by Rajya Sabha Chairman or Lok Sabha Speaker as the case may be.

Above mentioned are few of the such committees of Govt. of India who help in better policy making of scrutiny of the decisions taken by the various ministries or departments.

COMPTROLLER AND AUDITOR GENERAL OF INDIA

Introduction: The power of accounting and audit is vested in the Indian Audit and Accounts Department which is headed by the Comptroller and Auditor General of India. This office came into being in 1919 when the first Auditor General was appointed by the Secretary of State. The Auditor General was responsible to the Secretary of State and held office during his Majesty's pleasure, He was thus made independent of the government of India whose accounts he had to audit. He was given constitutional recognition under the Government of India Act, 1935. The Constitution of free India, under Article 148, makes provision for such office re-designated as the Comptroller and Auditor General of India.

The Comptroller and Auditor General is the Head of Indian Audit and Account department. He is custodian of Public Finance and he is to see that not even a paisa is spent; without the authority of the Parliament. In order to perform his functions necessary that he should be independent of the executive. He has accordingly, been given a status equal to that of the judge of the Supreme Court.

Appointment and Conditions of Service: The Constitution of India lays down that :

1. There shall be Comptroller and Auditor General of India who shall be appointed by the President by warrant under his hand and seal and shall only be removed from office in like manner and on the like grounds as a judge of Supreme Court. In 1972, Amendment to the Act states that he should be appointed for 6 years or 65 years of age, whichever is first.
2. Every person appointed to be the Comptroller and Auditor General of India shall, before he enters his office, make and subscribe before the President or some persons appointed in that behalf by him, an oath or affirmation according to the form set out for the purpose in the Third Schedule.
3. The salary and other conditions of service of the Comptroller and Auditor General shall be such as may be determined by Parliament by law and, until they are so determined shall be specified in the Second Schedule Provided that neither the salary of a Comptroller and Auditor General nor his rights in respect of leave and absence, pension or age of retirement shall be varied to his disadvantages after his appointment.
4. The Comptroller and Auditor General shall not be eligible for further office either under the Government of India or under the government of any state after he has ceased to hold his office.
5. Subject to the provisions of the Constitution and of any law made by

Parliament the conditions of service of persons serving in the Indian Audit and Accounts Department and administrative powers of the Comptroller and Auditor General shall be such as may be prescribed by rules made by the President after consultation with the Comptroller and Auditor General.

6. The administrative expenses of the office of the Comptroller and Auditor General including all salaries, allowances and pensions payable to or in respect of persons serving in that office, shall be charged upon the Consolidated Fund of India.

The Comptroller and Auditor General of India is the administrative head of the Indian Audit and Accounts Department. The constitution laid down that: "The Comptroller and Auditor General shall perform such duties and exercise such powers in relation to the accounts of the Union and of the States and of any other authority or body as may be prescribed by or under any law made by Parliament and until provision in that behalf so made shall perform such duties and exercise such powers in relation to the 'accounts of the Union and of the States as were conferred on or exercised by the Auditor General of India immediately before the commencement of this Constitution in relation to the accounts of the Dominion of India and of the Provinces respectively.

It was in March, 1976 that the President of India issued an ordinance relieving him of the responsibility of compiling the accounts of the Union and the States at once or through stages. The ordinance was replaced by Comptroller and Auditor General Act 1976. The Act separated Audit from Accounts both at the centre and in the States.

The Auditor General conducts audit of expenditure, audit against Rules and Orders (Audit against Regularity), and Audit against Propriety.

Audit of Expenditure : It consists in examining whether the following essential conditions have been fulfilled :

- (a) that the expenditure is covered by sanction whether special or general accorded by competent authorities;
- (b) that it conforms to the relevant provisions of the constitution or laws there under, and with financial rules and regulations framed by the competent authority;
- (c) that it is covered by provision of funds authorised by the competent authority and is within the purpose for which the grant was intended to provide;

Why Comptroller and Auditor General should be appointed, is a question which has been well-answered by G.N. Joshi, in the following words :

"For effective and responsible government it is not enough that revenue should be raised and spent under the authority of legislature, it is also essential that the items of expenditure incurred by the executive should be kept strictly within the grants made by the legislature. This function is performed by Comptroller and Auditor General who is appointed to central, on behalf of the Union of the States, all

disbursement and to audit all accounts of moneys administered by and under the authority of Parliament and State Legislatures.

The provision about his appointment has been made in Article 148 of the constitution of India/He is appointed by President of India by warrant under his hand and seal. The person so appointed has to take an oath mentioned in the Third Schedule. His independence is essential, because his job is very unpleasant. He might displease many, while performing his duties. The result is that his removal has been made very difficult. He can be removed from office in a like manner and on the like grounds as a judge of the Supreme Court. It means that he cannot be removed by an executive order. His conditions of service cannot be changed to his disadvantages during his tenure. His salary, allowances and pension are charged upon Consolidated Fund of India and are non - voteable. After his retirement, he is not eligible to be appointed to any government office. His conduct be discussed on the floor of the House. The above provisions make his office exalted and independent.

Functions of Comptroller and Auditor General of India

He is required to perform such duties and powers in relation to the accounts of the Union and the States and of any other authority as may be determined by the Parliament. His functions may be mentioned as follows :

1. He is to take care that requirements of the law as to the issue of public money are being observed.
2. He is to see that the money is applied to the same purpose for which it was sanctioned.
3. It is his duty to check that expenditure should be supported by necessary sanction and documents.
4. He takes care that expenses voted by the Parliament and the State Legislatures are not exceeded or have varied from the original.
5. His duty is to see that accounts are properly maintained. He prescribes the form also in which the accounts are to be mentioned.
6. He is to assist the Central and State Governments, in preparation of annual financial statements.
7. He is to co-operate with different departments in the matter of maintaining their accounts.
8. He is required to audit all the financial transactions of the Government of India and Governments of States.
9. He is to control all disbursements, on behalf of the Union of the States,

The functions of the Comptroller and Auditor General of India are analogous to its counterpart in the U.S.A. Encyclopedia Britannica has mentioned the following functions of the Comptroller General of U.S.A.

1. He is responsible for performing grant wise audit of receipts and expenditures and use of public funds.

2. He prescribes principles for accounting to be observed by the executive agencies.
3. He is to co-operate with other agencies in developing their accounting systems.
4. He renders legal decisions pertaining to Government matters.
5. He reports the matters to the Congress.

Position of Comptroller and Auditor General of India

The office of the Comptroller and Auditor General is an exalted one. His appointment by the President makes his office of high status. His reports relating to the accounts of the union are submitted to the President, who causes them to be.

Role of Comptroller as AG :

As such, we see that the Comptroller and Auditor General of India plays a very important role and act as 'extended arm' of Parliament in controlling public expenditure. His report is based on factual date. It is because he is independent and free from any political pressure. Sitaramayya remarks.: "The C and AG today has been installed as a supreme master who has his own judgment to look to and who has no flaws or favors to be guided from any outside." Durell says: "The C.A.G. is the agent or Parliament. He is Parliament. Parliament only works through him." This is indeed an exaggerated view. T.G. Bowler calls him the "acting hand of the committee: of Public Accounts. He advises the committee and helps it extract right type of replies from the officials who are called to defend audit objections."

Appleby's criticism on C.A.G.

Paul H. Appleby, an American expert on Public Administration who was invited by the Govt. of India to examine our administration severely criticised our audit system in his report. "Re-examination of Indian administration system." He suggested that the office of the Comptroller and Auditor General should be abolished. His thesis is that the office of the Comptroller and Auditor General is in a large measure of inheritance from colonial rule, the Comptroller and Auditor General is a primary cause of wide spread and paralysing unwillingness to decide and to act; auditors do not know and cannot be expected to know much about good administration; their prestige is the highest, with others who do not know much about administration; auditing is highly pedestrian function with a narrow perspective and very limited use-fulness; the Deputy Secretary knows vastly more about significant problems in his Ministry than the entire Comptroller and Auditor General can discover by auditing.

Ashok Chanda commented on the points of the Appleby report and said "Appleby seems allergic to audit which he describes as 'highly pedestrian function with a narrow perspective and very limited usefulness. This attitude of mind has obviously coloured his observations on the Indian Audit organisation" Ashok Chanda referred to the increasing role of the Audit in U.S.A and U.K. and felt that Appleby's criticism was unduly severe. Ashok Chanda observes that in all recognised

democracies, Audit is not just tolerated as a necessary evil but is looked upon as a valued ally, which brings to notice procedural and technical irregularities and lapses on the part of individuals, whether they be errors of judgment, negligence, or acts and intents of dishonesty.

SUGGESTED READINGS

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6. Jones W.H. Morris: Indian Administration and Parliament in India
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LESSON NO. 2.7

CENTRE-STATE FINANCIAL RELATIONS IN INDIA

You have already studied the character and nature of Indian Federalism in the previous year. Now, in this lesson we shall discuss financial relations between the Centre and the State.

In a Federation, legislative relations between the federating units are wholly dependent on the division of powers made by the Constitutions itself. Two practices are generally adopted and one is that of United States of America. There, the Constitution has clearly specified the powers of the federal government and all the remaining powers are given to the federating units. This method usually results into federation with weak centre. And then there is Canadian model, according to which the powers of the units are clearly demarcated and all the residuary powers are with the centre. The result is a highly centralised federation. India has not adopted any of these practices, though Indian federation is also a centralised one like that of Canada. Infact, Indian federation has got certain peculiar characteristics of its own which we had to adopt taking instance from our past history. In the beginning of the British rule in India, the central government was given too many powers, but soon the policy of decentralisation was adopted which culminated into the Government of India Act, 1935.

The Act attempted at solving two major problems of India i.e. that of princely states and communalism by creating a federation. Though the federation as provided for in this act, could not be established; yet the division of subjects as provided in the act served as an ideal for the Constitution makers of Indian Republic. Like the Act of 1935, the new Constitution provides for three legislative lists in the Constitutions i.e. Union List, State list and Concurrent list. As all the residuary powers have been vested with the centre, some people are of the opinion that only state list and concurrent list should have been specified and the residuary power should have been left with the Centre. But the Drafting Committee was of the opinion that the three detailed lists would prevent the possibility of all those disputes between the federating units which were likely to arise due to vague statement of their legislative powers in the constitution itself. This is a general defect of federal government, specially that of Canadian federation. One thing must be kept in mind that the question as to how the division of powers should be made and whether the residuary powers should be vested in the Centre or the States can be solved only after keeping in view the particular political background of a country. For Example, in United States of America though small states aspired for federation, they never liked complete subordination to the centre. They were of the opinion that those matters which concerned them all should be entrusted to the centre and all other should be left to

them. For this very reason only the list of the legislative powers of the federal government is included in the American constitution and the residuary powers are left to the units. Our constitution makers were well aware of the defects of a weak Centre, as there are so many instances of disintegration in our history due to a weak government at the Centre. So, a strong centre was preferred.

Division of Powers Under the Indian Constitution

Indian federation is characterised by a high degree of centralisation. This is made unmistakably clear by three lists contained in the seventh schedule and other provisions of the Constitution.

Union List : This list contains 97 items and is thus longest of the three. The Union Parliament has the exclusive authority to frame laws on subjects enumerated in this list. The list contains subjects like Foreign affairs, Defence and Armed forces, War and peace, atomic energy and natural resources necessary for its production, posts and Telegraph, Foreign Trade, Interstate Commerce, Banking, insurance and interstate rivers etc.

State List : The State list consisting of 66 items contain subjects on which ordinarily, the State alone can make laws. In other words, these subjects are outside the legislative jurisdiction of the Parliament under normal circumstances. Included among these subjects are Public health and Sanitation, Education etc. The subjects enumerated in State list indicate a substantial field of local action. What makes the State autonomy less real than it appears at a first glance, is the fact, that under certain conditions the Constitution authorises the Union Government to extend its jurisdiction over matter formally included in the State list. Article 249 empowers the Rajya Sabha (Council of States) to transfer for a year at a time any matter in the State list to the legislative jurisdiction of Parliament by a resolution passed by a two-third majority. Article 250 empowers Parliament to legislate with respect to any matter in the State list during the operation of the proclamation of Emergency. Such a Law is valid during the emergency and even six months after that.

According to Article 252, Parliament acquires the right to legislate on any subject in the State List, if the legislatures of two or more states resolve to make a request to Parliament to that effect. The laws so made by the Parliament can also apply to other states which may adopt them after expressing their request in the same manner.

Article 253 empowers Parliament to make any law for the whole or any part of the territory of India for implementing any treaty, agreement or convention with any other country or countries or any decision made at any international conference, association or body.

Concurrent List

This list consists of 47 subjects, both the Union Parliament and State Legislatures can make law on subjects given in the Concurrent List. The Concurrent List is, in fact, a device to avoid the rigidity of distribution of subjects under two lists which tends to place the power of the centre and the units in water-tight compartments.

The possibility of interference into each others sphere increases due to Concurrent List because it consists of such subjects on which both can frame laws and due to this there can be conflicts regarding jurisdiction. The Concurrent list consisted of such subjects which are to some extent related to the local or national interest such as criminal laws procedure, civil procedure, marriage and divorce, economic and social planning, trade unions, labour welfare and so on. Though both Parliament and State legislatures have concurrent powers as regards this list yet in case of a conflict, the central law must to the extent of repugnancy, prevail over the state law. If however, the state law has received President's assent, it will prevail over the central law unless and until Parliament passes a new law overruling the provisions of the state law. Thus, in case of the conflict over concurrent subjects, the position of the Centre is far more stronger than States.

Residuary Power : All residuary powers i.e. the powers not specifically included in the three lists have been placed under the legislative jurisdiction of the Union Parliament. This is yet another departure from the normal pattern of federalism. In U.S.A. Switzerland and Australia, residuary powers have been vested in the competent units. Under the Government of India Act 1935, these powers were not given to any of the federating units and Governor General had the power to entrust them to any of the two according to the requirement of the time.

The above given plan for the division of the legislative powers clearly indicates the high degree of centralisation. The reason for adopting such a plan seems to be the over-increasing trend of the world federation towards the centralisation. This division of power has also been criticised for being a departure from the true federal principles. Upto fourth general elections there were almost no problems in its actual working because of the same ruling party at the centre and state level. But after the Fourth General Elections, controversy over centre's overlordship was raised as non-congress government came into power in number of the States of Indian Union. Some of the state governments were strongly opposed to the policies of Central Government. The result was an open conflict on many issues between Centre and the States. These governments, specially those of Communists and D.M.K. parties. raised the issues of redistribution of powers and demanded more powers for the states.

After the Fifth General Elections, the Congress has regained the majority at the Centre as well as in the most of the States of the Indian Union. So, the controversy regarding the readjustment of the relations seemed to have subsided for the time being. The centre had once again become as powerful as it was before the Fourth General Elections and the states, most of them having congress governments, now depended on the guidance of the Centre even in matters of state administration.

Keeping in view the above situation, some of the critics have compared the State Governments to "glorified municipalities", This charge is levelled due to the provision of Articles 249-253. These articles confer power on Parliament to enact laws on state subjects and therefore can interfere in the sphere of state administration. It is therefore

obvious that Parliament of India can legislate on the subjects falling within the State List. With regard to concurrent list, the Centre and the States both have the right to frame laws. In case of conflict over the jurisdiction of Union law and State law, the Union law shall prevail.

Although provisions made under the Articles 249-253 are not a regular features of the Federation yet India has laid down a new tradition by including them in the constitution. Our constitution was framed at such a time when the trend was for making the Central government strong. The Constitution makers, therefore, preferred to include the provision of this effect. Despite all this, to call the state as "Glorified Municipalities" is to underestimate their position. We should not forget that it is through the constitution only that Parliament has acquired the right to legislate on the subjects enjoined in the State List and it cannot interfere in any matter which may be against the Constitution. So it is more correct to call the states as units of a federal state rather than of unitary one.

FINANCIAL RELATIONS

As you know, India is a federal state and in a federation, the sources of income are divided between the Union and the States. Articles 268 to 291 of the Indian Constitution divides the sources of income between the Union and States, but the division is done in such manner that the States have to depend on the Centre i.e. Union Government. Those heads of income which have been allotted to the States, the revenue collected from them goes to the states concerned. But most of the money coming out of the sources given in the Union is also distributed among the states. The constitution contains a clear-cut bifurcation of taxes to be levied by the centre and the states. As the sources of income of the states were not sufficient, they have to depend upon the Union.

MAIN SOURCES OF REVENUE OF THE UNION

The distribution of the powers of revenue is laid down in the lists given in the seventh schedule of the constitution and the general pattern is based largely on the scheme embodied in the Government of India Act of 1935. The Union Government has an exclusive jurisdiction over taxes enumerated in the Union List. The concurrent list, however, includes no taxes. One important point to note here is that while the States retain the entire proceeds of taxes placed directly under their jurisdiction, the proceeds of source of some of the taxes in the Union List go wholly or in part to the States.

Taxes imposed by the Centre

Union list specifically mentions income tax (excluding agricultural income tax but including super tax, capital gains-tax, excess profit tax); custom duties etc.; excise duties excluding those which are put in the State List, estate duty goods and passengers carried by the railways; inter-state sales tax (only after the sixth amendment) and sales-tax on sale or purchase of newspapers etc. Parliament has jurisdiction to impose a tax in exercise of the residuary power. The scope of taxing powers of the

Union is further widened under the provisions of Article 252. Under the Article, a state may empower the centre to levy any tax coming under the state list.

The basic principles that guide the allocation of resources between the federation and the units are efficiency, adequacy and suitability. It is indeed difficult to achieve all the three ends at the same time. Constitutional, natural and economic considerations often stand in the way. Even if a certain system might suggest itself as the most acceptable, it would not satisfy the claims and counter-claims of the various States. Hence, the Constitution has attempted a compromise. According to this, the subject is divided into two parts, namely, (1) the allocation of revenues between the Union and the States, and (2) the distribution of grants-in-aid. The following list will show the respective sources of revenue for the Union and the States :-

(1) UNION SOURCES

1. Corporation tax.
2. Currency, coinage and legal tender; foreign exchange
3. Duties of customs including export duties.
4. Duties of excise on tobacco and certain goods manufactured or produced in India.
5. Estate duty in respect of property other than agricultural land.
6. Fees in respect of any of the matters in the Union List, but not including any fees taken in any court.
7. Foreign Loans.
8. Lotteries organised by the Government of India or the Government of a State.
9. Post Office Savings Bank.
10. Posts and Telegraphs; Telephones, Wireless Broadcasting and other like forms of communication.
11. Property of the Union.
12. Public Debt of the Union.
13. Railways.
14. Rates of stamp duty in respect of Bills of Exchange, Cheques, Promissory Notes, etc.
15. Reserve Bank of India.
16. Taxes on income other than agricultural income.
17. Taxes on the capital value of the assets, exclusive of agricultural land, of individuals and companies.
18. Taxes other than stamp duties on transactions in stock exchanges and future markets.
19. Taxes on the sale or purchase of newspapers and on advertisements published therein.
20. Terminal taxes on goods or passengers, carried by railways, sea or air.

Taxes Imposed by the States

The state list includes land revenue : Taxes on agricultural land and income tax and duties of excise on alcoholic liquors for human consumption, opium, hemp, etc. excluding medicinal and toilet preparations; octroi; sales tax in respect of, interstate sales and purchases of goods other than newspaper etc. Besides these, the states can earn additional revenue for business and factories. In some states, the Bus service is run either solely or to some extent jointly with other states and the revenue coming out of these is appropriated according to the shares of each state.

STATE SOURCES

1. Capitation taxes.
2. Duties in respect of succession to agricultural land.
3. Duties of excise on certain goods produced or manufactured in the States, such as, alcoholic liquids, opium, etc.
4. Estate duty in respect of agricultural land.
5. Fees in respect of any of the matters in the State List, but not including fees taken in any court.
6. Land Revenue.
7. Rates of stamp duty in respect of documents other than those specified in the Union List.
8. Taxes on agricultural income.
9. Taxes on land and buildings.
10. Taxes on mineral rights, subject to limitations imposed by parliament relating to mineral development.
11. Taxes on the consumption or sale of electricity.
12. Taxes on the entry of goods into a local area for consumption, use or sale therein.
13. Taxes on the sale and purchase of goods other than newspapers.
14. Taxes on advertisements other than those published in newspapers.
15. Taxes on goods and passengers carried by road or on inland waterways.
16. Taxes on vehicles.
17. Taxes on animals and boats.
18. Taxes on professions, trades, callings and employments.
19. Taxes on luxuries, including taxes on entertainments, amusements, betting and gambling.
20. Tolls.

DISTRIBUTION OF TAXES BETWEEN THE CENTRE AND THE STATES

The sources of income for the states from taxes and other business are too meagre to pay proper attention to the development of education, health, agriculture, social welfare, etc. which need more finances. To give the states sufficient money to run their administration smoothly, the Union Government gives some part of its income to

the States. The Constitution mentions four different categories of such taxes :

1. Firstly, there are some taxes which are levied by the centre but are collected and appropriated by states. These taxes are stamp duties, excise on toilet preparations and medicines containing alcohol etc. These items are included in the Union list but duties on these items are collected by the States and form a part of the revenue of the state which collected them.
2. In the second place, certain taxes such as duties in respect of succession to property other than agricultural land, estate duties in respect of property other than agricultural land, taxes on railway fares are levied by the central government and are collected by it. However the proceeds of these taxes are assigned to the states.
3. In the third place, income tax is levied and collected by the Union but shared between the Union government and the states.
4. In the fourth place, Parliament may provide that certain taxes such as excise duties other than those on medicinal and toilet preparations which are levied and collected by the Union and be also shared between the centre and the states.

Grants-in-Aid

In addition to the above schemes of distribution of taxes between the Union and the States, the Constitution provides that Parliament may by law give grants in-aid to the needy states out of the revenue of the central government. The amount of the grant is to be determined by Parliament and therefore, no uniform policy may be adopted in giving these grants to the states and the quantum would depend upon the peculiar need of the state.

- (i) Besides, the Constitution also lays down that the expenditure (or cost) incurred by State on the schemes for the welfare of the scheduled tribes is to be met by the Central government provided such schemes have been undertaken with the approval of the government of India.
- (ii) The Assam government gets economic grant-in-aid for the development of the Tribal Area in the State.
- (iii) The States of Bihar, Orissa and West Bengal get economic grants from the Union Governments, can take loan against the securities of their consolidated Funds. However, the extent of the loan is to be determined by the respective Legislatures.

Central control over States

As source of income for the states are limited and therefore, they have to look upto the centre for getting necessary funds to undertake schemes of development etc. K. Santhanam has rightly compared states as beggars at the foot-doors of the centre government. For enabling the states to undertake schemes of Public Welfare, the states need more funds so that they may carry out their responsibilities to their people. The Planning Commission has come to occupy unique importance in our country and the

states are asked to carry out plans even though the states may be expressing their unwillingness. Although education, agriculture, medicines, cooperatives and social welfare subjects fall with the state List, yet these subjects are being controlled by the Union Government through the policies of the Planning Commission. After every five years, the President appoints a Finance Commission to analyse the Financial relations between the centre and the states. It makes suitable recommendations for adjustment of resources and lays down procedure for giving grants to the states. It may be noted that the Planning Commission has also acquired the power to give grants to the States irrespective of the recommendation of the Finance Commission. This results in confusion and is source of friction between the centre and the states. Central Government through the agency of Planning Commission has encroached upon the autonomy of States. Shri Ashok Chanda, the Ex-Controller and Auditor General of India, gives his own reason for this type of situation. He is of the view that states depend upon the centre for every thing. They seek the help of the centre for every project. States do not levy any special taxes nor do they control the expenditure. He feels that unless the states are made financially independent, they will not feel their responsibility properly. He further suggests that the Planning Commission should not make plans for the states. State should raise revenue within their own needs and necessities and will then examine the sources of their revenues. Central Government should come forward to help the states as and when emergency arises.

Financial Emergency

During the period when the proclamation relating to Financial Emergency is in operation, the executive authority of the Union extends to the giving of directions to any state to observe such canons of financial propriety as may be specified in the direction or India. Such directions in the constitution may (a) ask state to reduce salaries and allowances of all or any class of public servants with the affairs of a state.

(b) Reserve all money Bills for the consideration of the President after they have been passed by the state Legislature.

2. While the Proclamation of Financial Emergency is in operation, the President is competent to issue directions for the reduction of salaries and allowances of all or any class of persons including the judges of the Supreme Court and High Courts. **Financial Emergency so far has never been imposed.**

FINANCE COMMISSION

Having in mind, the far-reaching importance of the working of the Indian Federal system, there is a provision for Financial Commission in the Constitution. The President of India is required under article 280 of the Constitution to set up, within two years from the commencement of the constitution and thereafter, every five year or earlier a Financial Commission consisting of a Chairman and four members. The Finance Commission is a unique feature in the Indian Federal Structure which is not found elsewhere. It is something like the State Grants Commission in Australia.

The Eleven Finance Commissions so far have been constituted by the President in (1951, 1956, 1960, 1964, 1968, 1972, 1977, 1982, 1987, 1992, 1997 etc). Eleventh Finance Commission submitted its report on July, 28, 2000 to the Govt. which has been accepted. As a result of the recommendations of these Commissions, the State's share of the proceeds of income tax have been steadily increasing. The First Finance Commission 'broke new ground' by recommending that 40% of the net proceeds of union excise duties on three commodities (tobacco, matches and vegetables) should be distributed among the states. The second Financial Commission added five more commodities viz., sugar, tea, coffee, paper and vegetable oil and reduced the share of the states in the net proceeds of the duty on all the eight commodities to 25%. The third Finance Commission further increased the share of the states and the fourth commission recommended that all union excise duties currently levied should be shared between the centre and the states. The fifth Finance Commission was appointed under the Chairmanship of Mr. Tyagi and the purpose of its appointment was to consider the sources of income under the Fourth Five Year Plan. The eleventh Finance Commission was constituted under the Chairmanship of A.M. Khusro and the basic purpose of its appointment is to consider the sources of income under the 9th five year plan.

2. Finance commission recommends to the Centre for grant-in-aid to be given to the states. Before 1952 only nominal grant was used to be given to the states but now every Finance Commission has been making recommendations for granting as much aid as is possible. First Finance Commission recommended that grant of five crores to the states, the second made it 37 crores, the third 58 crores and the fourth 63.75 crores.

The fifth commission recommended grant for each year during the plan period on a steadying scale in diminishing quantum from about Rs. 153 crores in 1969-70 to 102 crores in 1973-74. However, Ninth & Tenth Finance Commission recommended Poverty, Population, Economic per capita income resources as criteria of distribution.

The Finance Commission have felt need for more resources of income for the state. That is why every Commission has recommended for as much grant and share of the production duty as possible. But they have also pointed out that the states are not trying to better the conditions for raising additional sources. Besides they are not controlling their expenditure. Because of these shortcomings, states depend upon the centre. This dependence upon the centre is responsible for making the position of the states very weak vis-a-vis the central government.

The function of the Finance Commission is to systematise the sources of income of the centre to the states. With the emergence of Planning Commission, the role of the Finance Commission has been undermined. The Planning Commission not only draws plans and policies for the states but also decides the extent of grants to be given to the state. As a result, these functions of the Finance Commission have been automatically

delegated to the Planning Commission. The Finance Commission now-a-days keeps in mind the needs of the Planning Commission and as such works on the lines as laid down by the Planning Commission.

Some writers describe the Finance Commission as the servant of Planning Commission. Though it is a bit exaggerated observation but the spheres of work of the two Commissions should be demarcated clearly. The third Finance Commission even recommended either to increase the scope of its functions, or to change Planning Commission itself and the rest of the Finance Commissions did not touch that controversial point. Now the Eleventh Finance Commission has the opinion to widen the role of Finance Commission but still its recommendations are going to be pending.

Criticism & Suggestion

From above discussion, it is clear that in India, centre enjoys more power as compared to the states. In other federations of the world, there has been a little hesitation to strengthen the hands of the Federal Government vis-a-vis the states. In the U.S.A. the centre does not have any power to give instructions to the States. In Australia, there is no such provision. The Framers of Indian Constitution had the aim of 'unity in diversity' in their minds. They were conscious of the fact that federalism gives rise to legal dispute and weakens the unity of the country. Keeping in view the circumstances in which India got her independence, it became necessary that such special provision should be made to strengthen the unity. To keep this unity intact, the Union was given special powers through which the states were kept under its control. Prof. Paul Appleby, after studying the Indian administrative system, called the 'control' of centre as 'influence' as it is used through plans, conferences and ordinances.

After going through the administrative relations between the centre and the states, we notice that Indian constitutions has given many administrative powers to the centre. Articles 256 and 257 mentioned the provisions to exercise administrative control over the states. These provisions have been criticised on the ground that they vest administrative powers with the centre. Article 356 gives direct power to curb the independence of the states.

Another case of this criticism is the existence of All India Services as the state services and their role. Some states criticise the very existence of All India Services on the basis that in the federal state, the division of power and jurisdiction is already determined by the constitution. Hence, there is no need to have All India Services as the state services can serve the purpose. The states are also sceptical about the role of All India Services as the later are biased towards the centre. But so far the All India Services have given ample proof of their impartiality. They have been faithfully serving the state government. Constitution of India in itself is a cause of friction between the centre and states, its unitary bias is at the root of misunderstandings. There has been a demand especially from the south for change in the constitution and more powers for the states.

Another cause of friction between the centre and states has been the problem of maintenance of peace and order in the States. During the days of United Front Ministry in West Bengal the Union Government, against the wishes of the State government, sent its own reserve police force for the protection of its property. In 1968, the Communist Government of Kerala did not carry out the instructions from the Central Government concerning the suppression of strike by the employees of the Central Government. There is no doubt that the constitutional provision giving right of direction and control over the states to the Union Government contains an element of possibility of mischief as this power may be abused unmindful of the autonomy of the states. There are instances where the Central Government interfered in the states to advance party interests. But we have to put up with this taking it as a 'necessary evil' when we find that a strong centre is needed in India to combat the disruptive and divisive forces and to maintain the unity and integrity of the country.

Conclusion & Evaluation

In this lesson, we discussed financial relations between the Union and States. We find that the constitution has made the Centre very strong. Not only that the Union has been given more subjects than the states, the Union Parliament under certain conditions is empowered to make laws on the state list. In concurrent list, too, the Union laws override the state laws. We have also found that the States have meagre resources and depend upon centre for financial help. This gives the Union Government an authority to direct and keep a check over the States. In the administrative field, there is a constitutional obligation on the State Government to ensure compliance with the laws made by the Parliament and not to impede or prejudice the exercise of executive power of the Union within their respective spheres. When both these provisions are put together they naturally widen the authority of the Union Government and restrict the executive authority of the States. The All India Services who run the show in the States as well to further strengthen the power of the Union Government and restrict the executive authority of the state strengthen the power of the Union Government. There has been a lot of criticism against the over-awing authority of the centre in a federal set-up. Some of the states in India are demanding more power and decrying the interference of the centre in the state affairs. But this criticism does not hold much better when we find that all over the world the trend is towards having a strong centre in both unitary and federal states.