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**Consultation on Role and Functions
Of
State Finance Commission**

Context

India's decentralization initiative in the form of 73rd and 74th Constitutional Amendments ensures constitutional validity to local bodies and has also broadened their range of power and functions. In this context, the provisions concerning the constitution of State Finance Commissions (SFCs) aiming to rationalize state- local fiscal relations, assume special significance.

In terms of articles 243(I) and 243(Y) of the constitution, the State Finance Commissions (SFC) are to recommend:

- (a) the principles that should govern the distribution between the state on the one hand and the local bodies on the other of the net proceeds of taxes etc. leviable by the state and the inter-se allocation between different panchayats and municipalities;
- (b) the determination of the taxes, duties, tolls and fees which may be assigned to, or appropriated by the local bodies; and
- (c) grants in aid from the consolidated fund of the state to the local bodies.

The SFCs are also required to suggest measures needed to improve the financial position of the panchayats and the municipalities.

The importance of the SFCs in the scheme of fiscal decentralization is that besides arbitrating on the claims to resources by the state government and the local bodies, their recommendations would impart greater stability and predictability to the transfer mechanism. However, the situation of SFCs leaves much to be desired. Usually their recommendations are not accepted without modifications and even the accepted recommendations are not fully implemented, citing resource constraints and this defeats the very purpose of constituting them. The 11th Finance Commission did not find the first generation of SFC report to be useful for its purposes.

In Gujarat too, the second SFC was constituted on 19th November 2003 i.e .five years after the first SFC submitted its recommendations that were accepted. No action has yet been taken by the Gujarat government to implement the accepted recommendations of the first SFC. The situation needed a change but over the years SFCs had remained institutions least discussed in civil society. Also, there was lack of understanding about its role, functions, importance and current status. A consultation was thus organized on 14th December 2005 to start a dialogue about this institution and think about ways for involvement of civil society to correct the situation and strengthen SFCs.

Consultation proceedings

After a round of introductions and outlining the context and objectives of the consultation by Director, Unnati – Organization for Development Education, Shri Manoj Rai from PRIA, Delhi briefly provided an overview of the status of State Finance Commissions across the nation, many a times comparing them with the Central Finance Commission. His major source of reference in this case was the dialogue between State Finance Commissions and the 12th Finance Commission organized in Delhi on 2nd December 2005. He informed the participants that the meeting had been appreciated for being the first of its kind that had representatives of State Finance Commissions (SFC) from 15 states. From the 15 states there were 8 Chairpersons, 3 Member-Secretaries and 4 Principal Secretaries of

SFCs. Dr. C. Rangarajan from Prime Minister's Economic Advisory Council and many senior representatives from Government of India were also present.

He categorically listed the problems plaguing SFCs as articulated by the representatives themselves under 5 'C's:

1. Constitution of SFCs – none of the SFCs were constituted in one go. First Chairperson was selected, then the members and by the time Chairperson and members met together, a year from the scheduled term of 2 to 2 ½ years is already over.
2. Composition – members are selected without consideration of qualification.
3. Continuity – SFC representatives of at least 4 states HP, MP, Orissa and UP said that there was lack of institutional memory and ad-hocism prevailed. There was no permanent secretary to take on the functions of recording, compiling or maintaining. The Central Finance Commission (CFC) has a specialized cell located in the Finance Ministry to cater to this purpose.
4. Consultation – Provision for SFC was made compulsory by the 73rd and 74th Constitutional Amendments and two Articles of our Constitution are devoted to it but this importance does not reflect in reality. SFCs do not consult panchayats and municipalities but CFC has a well-defined mechanism for this.
5. Convention – Perhaps lack of importance given to the Commission also results from the fact that the government is not bound to accept its recommendations. Only about 40% to 60% of recommendations are accepted and that too only those that could be called 'safe'. 'Action taken report' just mentions that the recommendation has been rejected but provides no logic for it.

There was a general consensus that the SFCs were over-burdened, as they also had to generate data before it could be available for analysis. Reinforcing the non-availability of data, Shri Manoj Rai quoted what Dr. Rangarajan had said during the consultation in Delhi. He had said that SFCs to function effectively only needed information about two things, i.e., state expenses and local bodies expenses and work in reverse for estimating the need for revenue, but even data about these was not available. He had voiced a need for forming a Forum of and for SFCs so that their hands were strengthened. He had also stated that as per the provisions of Article 280, SFCs should discuss tax sharing between state and local bodies or go in for Constitutional Amendment though that would defeat the purpose.

Dr. S.S. Mehta as the next speaker built the authenticity of his arguments by informing about his background of association with several important state-level committees. He emphatically said that data was available for functioning of SFC in Gujarat. Talking about the dire situation of SFC, he said that the 1st commission constituted in 1994 submitted its report in 1998 and that too partly while the 2nd Commission constituted in 2003 was still deliberating. He felt that this situation was because of the lack of conditionality or pressure. Making the submission of report a pre-requisite for sanction of grant would automatically correct the situation and make SFC a necessity for the State Government. There were some 'necessary conditions' and some 'sufficient conditions' that states had to fulfill for sanction of grants and he felt that the requirement was synchronization of CFC and SFC reports.

Alternately he felt that the pressure should be built from below and there should be a creation of demand by the panchayats.

Dr. Mehta felt that NGOs could play a very important role in generating awareness among the panchayats, helping them to analyze the scenario and thus generate pressure of demand from below. He expressed there should be pressure by the SFCs on the Center so that more money could come to the consolidated fund of the state. He then informed everybody that Gujarat had been allocated Rupees 193 crores for panchayats and two very apt formulas had been developed by CFC to aid allocation that should be adapted for allocation of funds in Gujarat.

Shri Ramesh Shah, representative from Western India Forum for Panchayati Raj (WIFPR) reflected sadly on the fact that the 11th finance grants had not yet reached the panchayats and that there was no idea about the status of 40% of the amount that had to be given to panchayats for data generation. He also informed the gathering that the 12th Finance Commission had allocated 25 crores to the state to be passed on to the panchayats and municipalities. Another matter of concern raised was that the Finance Commission does not know when Center releases grants.

Shri Bipinchandra Vaishnav, a retired IAS officer and an expert on Panchayati Raj suggested that a small committee of four to five persons from the civil society should do concrete studies based on ground realities and then recommend to the SFC and the state government. He very strongly felt that the civil society should get together and move the courts for breach of constitutional mandate by the state government. He supported the view of Dr. Mehta that NGOs could play a very important role by having consultations with panchayats for generation of demand from below.

Shri Mahesh Singh, Joint Secretary, Urban Development Department shared the details of current status of allocations for the urban areas and said that a practice to link allocations to reforms undertaken to strengthen local bodies so that they are able to generate resources. As finance board had all data, it could be linked to the Finance Commission for providing data support. Chief Executive Officer of Gujarat Municipal Finance Corporation explained the financial status of the corporation and some initiatives taken to increase revenue generation.

Regarding future beneficial developments, representative from State Finance Commission informed the gathering that owing to development of online facilities, qualitative information could be directly gathered directly from Sarpanchs, status of village amenities (primarily in 78 areas) would be compiled every two years, 10 crucial amenities were to be identified and mapped at the taluka level through the use of remote sensing photos.

Outcome

A consensus emerged on the fact that in order to facilitate the process of much needed financial devolution, it was important to provide support to the SFC. It was also important to create an environment so that the state could appreciate the importance of the SFC in terms of its potential to carry the process of democratic decentralization further by strengthening the Panchayati Raj Institutions and Urban Local Bodies.

In the end it was agreed that it was necessary to build an image and legitimacy of State Finance Commission and generate bottom-up pressure on government.

State Election Commissions have got public legitimacy because of campaigns by civil society. Similar efforts needed to be made by the civil society for legitimacy to State Finance Commissions. NGOs could do active campaigning for generating awareness among the panchayats, helping them to analyze the scenario and thus generate pressure of demand from below for strength to SFCs. Another area where NGOs could be of help to SFCs was in providing and analyzing qualitative and authentic data from the field.

The state-level consultation on the 'Role and Functions of State Finance Commission' thus helped to bring a seldom discussed but important aspect onto the center stage. It also highlighted the importance of SFCs, the need to strengthen them and most importantly the role that civil society could play in that regard. It also opened a gate for future beneficial interactions between the civil society and the State Finance Commission.

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