

Financing Local Democracies: Panchayats and Multi-Level Federalism

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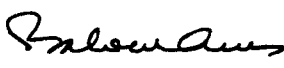



CENTRE FOR POLITICAL STUDIES
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DECLARATION

This is to certify that this Dissertation entitled "Financing Local Democracies: Panchayats and Multi-Level Federalism", submitted by Inoshi Sharma, for the award of Master of Philosophy is an original work and has not been previously submitted for this degree or any degree of this or any other University.

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July, 2002

Inoshi Sharma
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INTRODUCTION

India has great diversities in terms of culture, language, caste, group and economic stratification. Since independence continuous efforts have been made for development and welfare of the people of the Indian republic. Side by side the demands for eradication of poverty, disease and ignorance which are increasing in alarming proportions and require massive efforts is gaining momentum. This challenging task emphasizes economic priorities and the need to increase public participation to fulfill the rising expectations of the vast masses with a view to containing the forces of divisiveness. The emerging trend is tilting the balance towards decentralization¹. Local governments are not new to Indian culture rather they have been in existence since antiquity.

Contemporary Indian society through its democratic, republican and federal political set up has been striving for social, economic and political justice through modernization of its political and administrative institutions.

Rural self-government, both representative and responsive, has always been associated with democracy and development. The nature of Panchayati Raj institutions at the rural level in a country like India, the majority of whose population lives in villages and its dependence on agriculture, invariably decides the efficacy of the democratic system².

The hallmark of local government is its autonomy i.e. some power of direction. Decentralization should be both at the political and financial level.

¹ Wadhvani, M and SN Mishra, '*Democratic Decentralization: Objectives, Strategies and Future Challenges*', in Ministry of Rural Development, '*Renewing Local Self-Government in Rural India*', Occasional Papers-6, New Delhi, 1994, p.61

² Ahmed, RY, '*Panchayati Raj in Karnataka*', in Sebasti, L Raj SJ and Edward Mathias, ed. '*Peoples Power and Panchayati Raj-Theory and Practice*', ISS, New Delhi, 1998, Pp-170-171

Political authority without financial decentralization is completely meaningless. The finances of the local government institutions is a determinant in its functioning, there cannot be any local government without its own funds, budgets, income and planned expenditure. The economic dimension of local government lies in local levies – funds provided wholly or partially from among the beneficiaries.

Financial review years after working have revealed the weakness of income of the local government. Till 1992 there had been abysmal functioning of Panchayats due to less financial power and more social responsibility. Since independence the financial resource basis for local government had not been paid adequate attention. The 73rd Amendment Act 1992 through various articles sought to overcome this problem. The institution of Panchayati Raj is the reflection of India's faith in grass roots democracy. It is intended to involve local people in determining local priorities in development programs and enabling them to satisfy local basic needs which are universally considered as necessary to improve the quality of life³. It was considered as radical in nature, for it promised institutionalization of a third stratum of government at the local level. The implication of establishing institutions of self-government at the sub-state level has been, indeed, far reaching. It seemed that a decentralized polity was a distinct possibility in our country. In the political and economic spheres Panchayati Raj system has three main advantages⁴-

- a) People will have a better understanding of what the government proposes to do i.e. the Panchayati Raj system is an instrument of self-education,

³ Thimmiah, G. 'Keynote Address', in Konrad Adenauer Foundation, 'National Conference on Emerging Trends in Indian Local Government Finances, October 1996', Manohar, Hyderabad, 1998, p.20

⁴ Satya Sundaram, I, 'Power to the Powerless through Panchayati Raj', in Sebesti, L. Raj SJ and Edward Mathias, ed., 'Peoples Power and Panchayati Raj- Theory and Practice', ISS, New Delhi, 1998, p.19

- b) It helps to choose programs which serve the felt needs of the people, improve cost benefit analysis and bring about a radical social change, and
- c) The involvement of the people in the program of economic and social activities increases the likelihood of proper maintenance of such activities. If the people's participation in development is lacking, the bureaucracy becomes powerful and this leads to high incidents of financial leakages.

It is said the 73rd Constitutional Amendment Act of 1992 brought a revolutionary change in the political and financial structure of the rural local bodies. Financing Panchayati Raj Institutions has become a matter of great concern for all those who are interested in development welfare. This is because independence in raising and spending financial resources reduces dependence on higher levels of government and ensures autonomy in performance of functions.

The 73rd Amendment Act became a watershed in deepening democracy and the evolution of a third tier of constitutionally guaranteed stratum of government in the Indian federal system. The Panchayati Raj Institutions cover village, tehsil and district levels. If democracy means people's participation in running their affairs then it is no where more direct, clear and significant than at the local level, where the contact between the ruler and the ruled is more constant, vigilant and manageable. The grass-root level of democracy is the modern version of direct democracy, in huge countries like India with large population and regional variations, democracy to be meaningful and welfare-oriented implies decentralization. In a democracy, sovereignty should percolate from the higher apex of authority to the lower rungs of power. That is how it can be a "multiform democracy", which acquires its shape and form by becoming more inclusive and equalized by involving millions in their own affairs and for their own welfare⁵.

⁵ Khan, R, '*Federal India a Design for Change*', Vikas, New Delhi, 1992, p.89

The basic issue of inter-governmental transfers in the context of the constitutional amendments is or of rationalizing multi-level public finance planning and development in the Indian federal polity⁶.

State-local fiscal relations in India basically differ from federal-state fiscal relations in that local governments don't have specific revenue powers directly derived from the Constitution. They have to perform such functions and exercise such powers as maybe granted to them by the state legislatures⁷.

Three institutional features of the federal fiscal setting in India need to be made explicit at the outset because they are not necessarily common to all federal setting⁸-

- a) Inter-governmental transfers in India are unidirectional downwards.
- b) Although local governments are at the third tier and receive transfers from both the first (central) and second (state) tiers, central transfers are tied to particular programs principally for employment provision and carry no pre-determined annual regularity for any particular village Panchayats. State governments transfer by contrast carry annual regularity although within this category grants are more regularly disbursed than shared taxes.
- c) Third tier governance everywhere in India is not permitted to run a fiscal deficit.

Any machine runs on fuel or power, so also is finance for administrative machinery at centre, state or local government levels.

⁶ Oommen, TK, '*Panchayat Finances and Issues Relating to Intergovernmental Transfers*', in Oommen, TK, and Datta, A, '*Panchayats and their Finances*', Concept, 1995, p.1

⁷Subrahmanyam, K.Siva, '*Functional and Financial Devolution on PRIs, A Study in Andhra Pradesh*', NIRD, Hyderabad, 1999, p.3

⁸ Rajaraman, I and G. Vasishtha, '*Impact of Grants on Tax Efforts of Local Government*', Economic and Political Weekly, August 12, 2000, p.2943

Starved machinery at the feeble gears of economic activity cannot perform developmental works outright⁹.

More than eight long years have passed, but the change brought about by the Amendment has not been radical, nor are its implications found to be far reaching. For Panchayats have till now, failed to emerge as governments at the third stratum, up to the expected level. It is acknowledged by everyone that in the matter of distribution of powers and functions of the state, bias of the Constitution is towards the centre, there is much truth in the characterization of Indian state as quasi-federal¹⁰.

The problem arises when they are viewed as instruments for bringing about rural development, while the centre and states consider them as mere implementing agencies of programme prepared in distant Delhi or state capitals. The main questions regarding financial decentralization seem to be, 'is it possible to conduct a meaningful planning process from the bottom up (as the rhetoric requires, and the Constitution demands), when it seems clear that the resources will almost inevitably have to come from the top down?'. Is it possible to harmonize centrally sponsored schemes and state funded and implemented activities (particularly in education and health) on the one hand, and local preferences on the other, given the local dynamics of national and state level political (party) systems, and agenda, and local systems of power?¹¹.

Despite more than fifty years of independence, the administration in India is not fully 'developmental'. What has happened is that at the central and state levels, elected persons in command are effectively preventing democracy from reaching the district level and below. Obviously, in order

⁹ Mohanty, B, 'Non-Tax Revenue Generated by Local Governments', in Konrad Adenauer Foundation, 'National Conference on Emerging Trends in Indian Local Government Finances, October 1996', Manohar, New Delhi, 1998, p.166

¹⁰ NCRWC, 'A Consultation Paper on Review of the Working of the Constitutional Provisions for Decentralization', ncrwc@nic.in.com, para-1.1

¹¹ *Panchayati Raj Update*, ISS, May 2002, p.8

to be fully developmental, there has to be complete decentralization. Also, the inherent conflict between technical goals and parameters of human development and the 'politics' of dealing with citizens as human beings with aspirations, is not yet resolved¹².

The tragic part is that even under the new dispensation following the 73rd Amendment, there has not been much serious effort to maintain some measure of vertical fiscal balance in the division of functions and finances at the union, state and sub-state level. There is much ambivalence and mismatch at the PRI's level, the nature and magnitude of which varies from state to state. It is here that the question of evolving relevant principles and norms of transfer assumes significance. Economic efficiency and equity which are basic considerations in fiscal transfers must be kept fully in view with regards to sub-state level fiscal transfers as well. Clearly, some degree of inter-panchayat equity has to be ensured¹³.

REVIEW OF LITERATURE

For the purpose of carrying out this dissertation an attempt to make an exhaustive study of the existing literature on financing of Panchayats has been made. Both primary and secondary works were reviewed.

Mukarji and Arora (1992) provide an understanding of the working of the Indian federalism, the challenges it faces in contemporary times and the need for devolution of power and decentralization which would make India truly multi-federal.

Rai, et. al. (PRIA2001) traces the development of Panchayati Raj institutions in India since independence. It looks into the recommendations made by the various committees set up by the

¹² Ibid.

¹³ Oommen, TK, '*Panchayat Finances and Issues relating to Intergovernmental Transfers*', in Oommen, TK, and Datta, A, '*Panchayats and their Finances*', Concept, New Delhi, 1995, Pp.22-23

Government of India to strengthen Panchayats, highlights the problems they face and the ways and means to make them more secure.

Institute of Social Science (2000) provides a condensed overview of the status of Panchayati Raj institutions in States and Union Territories. Along with it, the National Institute of Public Finance and Policy (2000) have identified instances of deliberate oversight and negligence in setting up parallel structures which thwart the independent working of Panchayats.

The Rajiv Gandhi Foundation (1999) through its workshops in various parts of India sought to engage with the people's representatives at the grass-root level directly- to understand their problems and urge them to suggest ways to overcome those.

Konrad Adenauer Foundation (1998) organized two conferences in October and December 1996, on State-local fiscal relations in India, which provides the earliest attempt made, immediately after the passage of the State Conformity Acts by the States following the 73rd Amendment Act 1992, to discuss the problems of financing Panchayats and highlighted that the problems were mostly due to political rather than administrative and technical problems.

The Government of India recognizing these problems had in July, 2001, organized the State-Ministers conference on Panchayats. Subsequently the All India Panchayat Adhyakshas Sammelan, April 2002, was held where the issue of financial devolution and further administrative autonomy and therefore the need for restructuring of Panchayats including the option of further amending the Constitution was raised. National Commission to Review the Working of the Constitution (2001) in its paper on local bodies found the working of Panchayats more in keeping the letter rather than the spirit of the law.

The issue of financing of Panchayats has time and again also been raised in various newspapers and journals which have been looked into. As has been seen above there has been an overall consensus amongst

most works reviewed that the need has come after almost a decade since the Act was adopted, for a comprehensive study of the existing provisions for financing of Panchayats, their actual working and ways and means to overcome those problems. Without financial autonomy, the very working of Panchayats as the third stratum of Indian federal structure is doubtful. Financial autonomy is the sine qua non of the concept of autonomy and self-governance of local government in India.

OBJECTIVES

In the dissertation that follows, an attempt has been made to look into the issues related to the financing of Panchayats- the obstacles and achievements within the Indian federal setup in ensuring financial autonomy for local self-government bodies. The objective is to-

- Outline some of the conceptual and operational issues related to federalism, local-government and inter-governmental transfers of funds to the local-government,
- Review the existing structure of Panchayati Raj finances, challenges that they face in gaining financial autonomy (primarily political in nature) and the recommendations that have been made to strengthen their financial base.

In chapter 1 a cursory look at the meaning and development of the concepts of federalism and local-government and subsequently a historic perspective in order to understand the steps that have been taken in India to establish local self-government within the federal system has been made.

Chapter 2 makes an in-depth study of the constitutional provisions as well as the various sources of financing the Panchayati Raj institution and their financial position in various states.

Chapter 3 sees the financial constraints faced by the Panchayats and the limitations placed on the actual fiscal devolution on the PRIs

which greatly restricts their autonomy to act as institutions of self-government.

Chapter 4 looks into the recommendations made by various organizations to strengthen the finances of Panchayats including the views of the National Commission to Review the Working of the Constitution.

In conclusion, the recent central governments efforts to take into account different views of the varied sections in our society and to reiterate the pressing need for federal studies to go beyond the centre-state relation paradigm and the future potential of multi-level federalism has been made.

CHAPTER 1

EVOLUTION OF PANCHAYATS IN INDIAN FEDERAL SET UP

CONCEPT OF FEDERALISM

Every nation is more or less closely integrated in accordance with its own peculiar history, culture, economics, politics and other determinants. Diversities may be distributed such that they are found scattered widely or grouped territorially- in case of the latter, it provides a stimuli which results in a political organization that is 'federal'¹.

The term 'federal' is derived from the Latin word 'foedus' (covenant) which is used to describe the mode of political organization which unites separate polities within an overarching political system so as to allow each to maintain its fundamental political integrity².

Traditionally the notion of federalism has been understood as a step further than a confederation or loosely coordinated states created for the purpose of security or defense or for any other limited purpose. Federalism is the result of historical evolution. Some imminent crises, diplomatic move or allurements of major economic gains, danger of aggression or need of defense may also contribute to the taking of such coordinated steps involving both unity and diversity and give concrete shape and form to the polity of their choice³.

Federal political system refers to a broad category of political system in which, by contrast to the single central source of authority in unitary system, there are two or more levels of government. They thus combine elements of shared rule through common institutions and

¹Livingston, WS, '*Federalism and Constitutional Change*', Greenwood, Connecticut, 1974, Pp.4-5

²*International Encyclopedia of the Social Science*, Volume-5, McMillan Co. and Free Press, 1968, p.353

³Elazar, DJ, '*Exploring Federalism*', the University of Alabama Press, Tuscaloosa, 1987, Pp.5-6

regional self rule for the governments of the constituent units. It ensures that 'government at the constituent and central tiers always exists--- in federation the constituent units have agreed with each other that each will retain its identity and function'⁴. The field of government is so divided that the relationship between the general and regional government is not of subordination but coordinate with each other.

DEVELOPMENT OF LOCAL GOVERNMENT

There is nothing in the federal idea or in the various theories of federalism which limits its application to two levels of government only. It is believed that 'downward extension of the federal principle and flourishing democratic institutions would strengthen democratization at all levels'⁵. Thus to assume that state / regional units can be representative of all forms of regional interest over-simplifies the existing ground realities. Rather there has been a need for decentralization within these units to accommodate more 'local aspirations'⁶ and thus become truly multi-federal.

Local government is defined as a public organization authorized to decide and administer a limited range of public policies within a relatively small territory. Local government has its base in the locality, which means a limited area⁷. The local government within a defined area has the authority to undertake and power to perform public activities. The concept of local government needs to be emphasized in the modern context where the state with its multitudinous activities which affect all aspects of

⁴ Riker, WH, 'Federalism', in Goodin, RE and Philip Pettit, ed., 'A Companion to Political Philosophy', Blackwell, Cambridge, 1993, p.508

⁵ Mukarji, N and Arora, B, 'Introduction: The Basic Issues', in Mukarji, N and Arora, B, ed., 'Federalism in India', Centre for Policy Research, Vikas, New Delhi, 1992, p.17

⁶ Watts, RL, 'Administration in Federal Systems', Hutchinson Educational Limited, 1970, p.50

⁷ Maheshwari, S, 'Local Government in India', Orient Longman Limited, New Delhi, 1971, p.217

people's lives tends to become monolithic. The local government is concerned with the governance of a specific local area contributing a political sub-division of the state⁸. A small size is preferred as it keeps the government closer to the people and succeeds in securing people's active and widespread participation in the conduct of local affairs. One of the advantages of the multi-level government organization is that it promotes competition between governments in the supply of public services and helps improve efficiency in their design and delivery. Further it is also believed that the operation of multilevel governments in a country encourages governmental authority to reap the benefits of comparative advantage in production and supply of a variety of public and social goods to the voter citizen⁹.

According to Professor Wallace Oates the expounder of 'economic theory of decentralization', tastes and preferences of voter citizens in different parts of vast countries like Australia, Canada, USA and India differ and any political institutional setup which is created should try to satisfy the varying demands for public services in keeping with the diverse tastes and preferences of citizens¹⁰. This can only be done when we have decentralized government, which will supply the required public services, which would enable the society to achieve pareto optimum in the provision of public goods.

PANCHAYATS IN INDIA

Village communities which were characteristic of agrarian economies had existed from earliest times in different countries such as

⁸ Barnabas, AP and OP Bohra, '*Finances of Panchayati Raj Institutions*', NIPFP, New Delhi, 1995, p.1

⁹ Government of Karnataka, '*Report of the State Finance Commission*', 1996, p.14

¹⁰ Ibid. p.12

the- Russian 'Mir'; German 'Mark'; medieval British 'Manor'¹¹ etc. as well as the Indian 'Panchayats'.

The need now emerges to view the development of local self-government within the federal structure of India. India's federal democratic structure has three levels of governance- national or federal, state or regional and the grass-root level called the Panchayati Raj and Nagarpalikas. The Panchayati Raj system covers rural India- the village, the tehsil and district levels. Traditionally Panchayats have existed in India since ancient times going back well over 2500 years. The great empires of Indian history were all of the character possessing strong power centers but recognizing peripheries exercising power legitimately and fully responsible for local conditions¹². Etymologically 'Panchayats' means a council of five persons, which was the pivot of administration to manage the social life and economic activity.

By the 18th century the British colonialists had arrived and guided by purely administrative needs of a centralized colonial state, had institutionalized the district administration by the Government Resolution 1882 under Lord Ripon. Sir Charles Metcalfe called the village Panchayats as 'little republics', which lasted when nothing else could last¹³.

During the subsequent freedom national movement there was always an undercurrent favoring the establishment of a system that would restore the importance and autonomy to village community. A local community or a *gemeinschaft* is characterized by autonomy of decisions and actions and on this bedrock rests the strength and vitality of a nation. The sociological fact that a nation is a community of communities legitimizes a citizen's right to participate in the governance of

¹¹ Mathew, G, '*The Federal Principle in Local Government*', in Mukarji, N and Arora, B, op.cit, p.238

¹² Elazar, D, op.cit, Pp.193-194

¹³ Khan, R, '*Federal India a Design for Change*', Vikas, New Delhi, 1992, p.60

gemeinschaft¹⁴. Mahatma Gandhi understood this fundamental truth more than anyone within the Indian ethos. Along with other national leaders like Shri Rajendra Prasad, he advocated the primacy of village as the starting point of development.

With independence in 1947, owing to the existing circumstances i.e. earlier experience of partial federal working under Government of India Act 1935, need for stability and security in post-partition era and the need to integrate diverse regional interests and vast populace, made the framers adopt a federal system with a strong center. Fathers of the Indian Constitution firmly held the conviction that unity and integrity of the country should be maintained in the light of experience of history and expediency, the primary ultimate goal of our polity. In the Constituent Assembly Granville Austin and M M Sankhder found virtual unanimity in favor of a strong and overriding authority of the center¹⁵.

A unitary mindset appears to hold sway the Constituent Assembly and its mood was summed up by Dr. Ambedkar who on introducing the provisions of the Draft Constitution said, 'though the country and the people may be divided into different states for convenience of administration; the country is one integral whole under a single imperium derived from a single source'¹⁶. The issue of state and local rights was accorded a secondary status by the framers of the constitution. Many believed that local politics would encourage divisive trends. Even as the Constitution was being drafted; in his fortnightly letter to Chief Ministers, Pundit Nehru remarked '--first priority must be to preserve unity; strength and stability--- everything that comes in the way of that may prove

¹⁴ Mathew, G, op.cit. p.239

¹⁵ Verma, SL, '*Panchayati Raj and Gram Swaraj: Federalogical Considerations*', Verma, SL, ed., '*Panchayati Raj, Gram Swaraj and Federal Polity*', Rawat, Jaipur, 1990, p.23

¹⁶ Shastri, S, '*Local Democracy and Political Parties*', in Konrad Adenauer Foundation, '*Workshop on Political Parties and Party System*', Centre for Public Affairs, November, 2000, p.4

harmful¹⁷. For this purpose only two sets of governments were provided for. The Constitution describes India as a 'Union of States'. KC Wheare referred to this indigenously developed variant of federal system as 'quasi- federal'¹⁸.

Eventually, however as a concession to the Gandhian point of view regarding the village Panchayat as the foundation of self- government in India; the Constituent Assembly made a provision in Directive Principles of State Policy, Part IV, Article 40, which enjoins that Panchayats be endowed 'with such powers and authority as maybe necessary to enable them to function as units of self-government'¹⁹. As a result the State list included 'local government', which is to decide the structure and functions of local government. The history of independent India includes phases of interest in creation of strong rural local government institutions alternatively with their decline and dormancy.

PROGRESSIVE PHASES OF PANCAHAYATS

1947-1977

In the 1950s with the formation of the first 5-year plan, decentralization became important from the point of view of the twin objective of the Indian polity- democracy and development. The *raison d' etre* of the Community Development Programme launched on October 2nd 1952 was to better the economic life of the people. However it failed due to the 'conspicuous absence of people's participation'²⁰.

In 1957 the Team for the Study of Community Development Projects and National Extension Service under Balwant Rai Mehta as chairman to

¹⁷ Ibid.

¹⁸ Wheare, KC, '*Federal Government*', The English Language Book Society and Oxford University Press, 1971, p.28

¹⁹ Bakshi, PM, '*The Constitution of India*', Universal Law, New Delhi, 1998, p.72

²⁰ Mandal, A, '*Self-Government: Nomenclature for Panchayats*', IIPA, April-June, 1999, Pp.224-225

study and assess the extent to which the movement had succeeded in utilizing local initiatives and in creating institutions to ensure continuity in the process of improving economic and social conditions in rural areas, found that these programs had failed to evoke popular initiative and that Panchayats had not come into the field of community development in any significant way. It recommended the 'devolution of power to a body which when created— will have the entire charge of development works within it to itself the function of guidance--- and --- providing finance'²¹. It recommended the setting up of a three-tier structure with an organic link between the village, block and district levels. With this report the term 'Panchayati Raj' came into vogue conceptually as a process of governance 'even if only to handle rural development work only', were not implemented in all the states.

Subsequently the leadership that was emerging at the Panchayati Raj level which had a strong local identity and a better perception of local problems, came to be regarded as a potential threat by other levels of political leadership. If the leadership at the local level was different to that of the state, such difference was taken as a loss of power than a fact of political pluralism. The PRI structure thus did not develop the requisite democratic momentum and failed to cater to the needs of rural development. There are various reasons for such an outcome which includes political and bureaucratic resistance at the state level to share power and resources with local level institutions, domination of local elite over the major share of the benefits of welfare schemes, lack of capability at the local level and lack of political will. However non-devolution of sources of revenue proved to be the greatest stumbling block in the performance of these Panchayats²².

²¹Government of India, '*Report of the Team for the Study of Community Projects and National Extension Service*', 1957, Volume-1, p.7

²²Rai, M, M Nambiar, S Paul, SV Singh, SS Sahini, ed., '*The State of Panchayats-A Participatory Perspective*', PRIA\Sanskriti, New Delhi, 2001, p.7

The 1960s were a phase of neglect and decline of Panchayats in most states. The K. Santhanam Committee report on Panchayat Finance 1963 was the first committee to deal with the issues involved in strengthening the finances of Panchayats. This committee examined the various aspects of finances of Panchayats and made several recommendations for raising revenue from their own resources and the principles to govern devolution of various grants to the Panchayats from the State government. The Santhanam Committee Report 1963 had stated that, 'financial resources have to be adequate for the functions allotted to each Panchayat. No where in the world can local bodies function without substantial assistance from government. At the same time, it will detract from the dignity and autonomy of a self-governing institution if it is to be entirely dependent on assistance from above. It is essential for stability and growth of these institutions that they should have substantial and growing resources that are entirely within their power to exploit and to develop'²³.

1977-1992

By mid 1970's decentralization was almost reversed. The real control of funds and decision-making reverted to the state level leadership and the officials acting on their behest²⁴. It was thus seen that the concentration of function is greatest in the lowest tier of the system where finances and administrative personnel are invariably in shortest supply²⁵.

Indian politics showed a shift towards centralization. The emergency of 1975-1977 had made the federal arrangement into a 'Delhi-

²³ Oommen, TK, '*Panchayat Finances and Issues Relating to Inter-Governmental Transfers*', in Oommen, TK and Datta, A, '*Panchayats and their Finance*', Concept Publishing Co., 1995, p.4

²⁴ Sivaram Krishnan, KC, '*Power to the People? The Politics and Progress of Decentralization*', Centre for Policy Research, Konark, 2000, p.4

²⁵ Maddick, H, '*A Study of Rural Government in India*', Longman Group Limited, 1970, p.107

centric unitary system'²⁶. With the change of government at the center in 1977, a fresh attempt to examine and suggest measures to strengthen Panchayati Raj Institutions was made through the setting up of a 14-member committee under the chairmanship of Ashok Mehta on 12th December 1977. It stated that, 'as an end it (PRI) is an inevitable extension of democracy to the grass roots which in turn makes it the base of the democratic pyramid in the country'²⁷. Diagnosing the ills afflicting the PRI's the committee pointed out that haphazard programs, non-performance, rise of vested interests, lack of adequate financial resources etc. have positively contributed to its decline. However the committee also hastened to add that this failing was not peculiar to PRI's. It was only symptomatic of the decline afflicting the entire body politic of the nation. The committee represented a landmark in so far as²⁸-

- * it treated Panchayats clearly as an extension of democracy and recommended the establishment of democratic bodies below the state level,

- * declared the need of providing constitutional sanctions to Panchayats and

- * suggested "to transfer substantial quantum of powers from state government to local bodies".

Panchayati Raj was expected to build up not only a sound system of local self-government but also tackle the problem of building up democracy at the grassroots level and mobilize local human potentialities for rural development²⁹. The Committee found that it is generally the view that part of the inability of the Panchayati Raj institution to come up to the

²⁶Mukarji, N, 'Third Stratum', in Jha, SN and Mathur, PC, ed., 'Decentralization and Local Politics, Readings in Indian Government and Politics-2', Sage Publication, New Delhi, 1999, p.76

²⁷Jha, SN, and Mathur, PC, 'Introduction', in Jha, SN, and Mathur, PC, op.cit, p.35

²⁸ Ibid. Pp.23-24

²⁹ Bora, PM, 'Panchayati Raj and Democratic Aspirations of the People', Khadi Gramodyog, July, 1996, p.467

expectation lay in their 'weakness in financial resources'³⁰. Upon the review of the taxation powers and resources of the PRI, it found that in some cases they are too wide and incapable of meaningfully being utilized³¹. The Committee stated, 'we are interested in building the bridge between the developmental functions and financial decentralization which has been missing. For discharging the developmental responsibility entrusted to PRI, the state government should make commensurate funds from its total budget on a continuing basis. All PRI should have compulsory powers of taxation. The thesis, 'no taxation only representation' should be discouraged³². When a function is classified as implementation it should also be understood that the function entrusted to the Panchayats should have the money component with them³³. It found that the essential idea that all developmental activities should flow only through the block level organization had lost ground. Schemes like SFDA, DPAP, and ITDP etc. were not brought within the purview of the elected Zilla Parishad.

But the Committee did recognize the achievements of PRI's. Politically, it became a process of political seed drilling in Indian soil, making average citizen more conscious of his rights than before. Administratively, it had bridged the gulf between the bureaucratic elite and the people. From developmental angle, it helped the rural people cultivate a developmental psyche and socio-culturally it had generated a new leadership, which was not merely relatively young in age but also modernistic and pro-social change in outlook³⁴.

Being conscious of the operational realities of PRI's, the committee adopted a flexible approach to the problem and recommended a two-tier model of PRI. The Committee recommended that the first point of

³⁰Government of India, '*Report of the Committee on Panchayati Raj Institutions*', Ministry of Agriculture and Irrigation, 1978, p.102

³¹ Ibid. p.107

³² Ibid. p.125

³³ Ibid. p.63

decentralization below the state was suggested to be the district to be treated as a unit of planning. For the second tier, the committee thought in order to be a viable unit, the unit has to be bigger than existing Panchayats-suggested creation of Mandal Panchayats consisting of cluster of villages

The recommendations of the Committee were considered at the Conference of Chief Minister's in May 1979. But difference of opinion regarding structural pattern, state specific socio-cultural and politico-economic problems and the unwillingness of the ruling elite to share power at the district level and below, made it difficult to take off.

By the 1980s as in many other third world federations, in India too the problem of uneven development was being witnessed. Drain of country-side resources and impoverishment was leading to a vicious circle of under-development and migration from rural areas to the metropolis. In their masses, they overwhelmed the metropolis and transformed it into what has come to be known as the 'Calcutta syndrome'³⁵. But because of the existence of federalism, it was believed the new resources would inevitably spread over a number of centers.

Thus more people have a chance to benefit from development efforts. There was need to spread resources over a number of centers and to handle massive budgetary allocation for rural development and poverty-alleviation programme. This decade thus witnessed fresh efforts for a comprehensive look the at whole question of local self-government.

There was the resurgence of Panchayats in West- Bengal under the left government which had successfully launched 'Operation Bargha' to redistribute land by mobilizing the people at the grassroots level. Abdul Nazir Sab attaches great importance to the 'power of the people' slogan as a factor in the 1983 electoral triumph of the Janata party in Karnataka and recalls the model of a four pillar state (village-district-state-center)

³⁴ Ibid. p.5

³⁵ Elazar, DJ, op.cit, Pp.251-252

advocated by Mahatma Gandhi³⁶. A number of committees were subsequently set up which reiterated the need for setting up PRIs for the over all development of rural India and greater democratization of the political process. The need for financial autonomy and granting of constitutional status was emphasized. The GVK Rao committee 1985 sought to highlight the significance of -

(a)'decentralization at district level'³⁷ and below

(b) PRI has to be activated and provided with all the required support to become effective organizations

(c) The block development office should be the spinal chord of the rural development process³⁸.

LM Singhvi committee set up in 1986 reiterated the demand for 'constitutional protection of Panchayats as a third tier of government'³⁹. It suggested "..... a pattern of compulsory and optional levies and list of subjects of which power to levy taxes and fees may be entrusted to PRI with a provision that for a given period the state government shall levy and collect on behalf of PRI's and shall disburse to them on the basis of recommendations of the finance commission in each state".

The Sarkaria commission 1988, in its concluding chapter observed that the issue of devolution of powers and responsibility between the union and states must be considered in the context of 'broader issues of decentralization between these and other tiers of government on the one hand and the functional agencies within each of these tiers, on the other'⁴⁰.

³⁶ Arora, B, '*Federalism and Inter-Governmental Relations, A Bibliographical Essay*', in Bhatnagar, S, and Pradeep Kumar, ed. '*Some Issues in Contemporary Indian Politics*', Ess Ess Publication, New Delhi, 1993, p.67

³⁷ Ibid. p.59

³⁸ Rai, M, et al, op.cit, p.9

³⁹ Arora, B, '*Federalism and Inter-Governmental Relations in India*', op.cit, p.59

⁴⁰ Ibid.

By the end of 1988, a sub-committee of the consultative committee of Parliament for the Ministry of Rural Development under the chairmanship of P.K. Thungon made recommendations for the strengthening of PRI system. One of the important recommendations was that the Panchayati Raj bodies should be constitutionally recognized⁴¹.

It was against this backdrop that on 15th May 1989, the Government drafted and introduced the Constitution 64th Amendment bill in Parliament. But it could not be passed in the Parliament, as the state governments were being by-passed. The center had chosen to deal with bureaucracy in the states, district officers and chief secretary directly. Unprecedentedly, high amounts had been set aside for centrally sponsored schemes concerning state subjects and arrangements made for direct dispatch of funds to the district and direct submission of implementation reports to the centre⁴². The 64th Amendment bill was thus seen as a conspiracy for usurping the state government power and control over Panchayats.

73RD AMENDMENT ACT 1992

In the 1990s with the end of one-party dominance and pressure to decentralize the economic regime in the post-liberalization process, focus shifted towards reforms at the state levels. There was recognition that an increasingly global economy has itself unleashed economic and political forces strengthening both international and local pressures at the expense of the traditional nation-state. Global communication and consumership have awakened desire in the smallest and most remote villages around the world for access to the global market place; as a result governments have been faced increasingly with the desire for their people to be both

⁴¹Mathew, G, '*PRI in India- an Overview*', in ISS, '*Status of Panchayati Raj in States and Union Territories of India*', Concept Publishing Co., New Delhi, 2000, p.9

⁴²Sivaram Krishnan, KC, op.cit, p.8

global consumers and local citizens⁴³. In such a context federalism with its different interacting levels of governments, has provided a way of mediating the variety of global and local citizen preferences. Success of economic reforms is premised largely on the development of a decentralized federal democracy capable of providing effective initiative and governance at the state and local levels. The need was therefore to correct the malaise arising out of the 'reluctance' on the part of the states to accord to Panchayati Raj a place of 'political' importance and to devolve power and finances to these institutions⁴⁴. Abdul Nazir Sab, Minister for Panchayati Raj in Karnataka, in the 1980s had confessed, 'our intention to bring about a radical structural change in the governance of our state maybe laudable, but without a constitutional amendment guaranteeing the 'four-pillar state' our efforts may not be as fruitful as we desire'⁴⁵.

It took forty-three years since the Constitution of India was adopted for the local bodies in the country to become statutory bodies. The idea that produced the 73rd Amendment was not just a response to pressure from the grass roots, but to an increasing recognition that the institutional initiatives of the preceding decade had not delivered, that the extent of rural poverty was still much too large and thus the existing structure of government needed to be reformed. It was a political drive to see PRI's as a solution to the governmental crisis⁴⁶.

On December 22nd 1992, Parliament passed the Constitution (73rd Amendment) Act 1992 to, 'enshrine in the Constitution certain basic and

⁴³Watts, RL, '*Comparing Federal Systems*', McGill Queens University Press, 1999, Pp.4-5

⁴⁴Jha, SN and Mathur, PC, '*Introduction*', in Jha,SN and Mathur, PC, op.cit, p.24

⁴⁵ Mathew, G, '*Restructuring the Polity: the Panchayati Raj in Rajasthan*', in Sebesti, L Raj SJ and Edward Mathias, ed., '*Peoples Power and Panchayati Raj: Theory and Practice*', ISS, New Delhi, 1998, p.36

⁴⁶46 World Bank, '*Overview of Rural Decentralization, Volume- 3*', 2000, p.24

essential features of PRI to impart certainty, continuity and strength to them'. The bill got the President's assent on April 20th, 1993 and the Constitution 73rd Amendment Act came into effect from April 24th, 1993. For the first time the PRI system is sought to be given a proper statutory base within the Constitution. This would remove criticism that adequate constitutional sanction and structural legitimacy had not been provided to PRI's which was merely mentioned in the non-justiciable part of Constitution⁴⁷. The passage of the 73rd Amendment Act 1992 marks a new era in the federal democratic setup of the country and provides Constitutional status to PRI. Consequent upon its enactment almost all the states /UT's except J&K, NCT Delhi and Arunachal Pradesh have enacted their legislation. These Panchayats are being manned by about 34 lakhs elected representatives of Panchayats at all levels. This is the broadest representative base that exists in any country of the world⁴⁸. It was introduced to provide for democratic institutions, people's participation and opening the doors for reversal of the political system, which was till recently top heavy. What is different about 3-tier federal system is that sub-state structures are no longer simply creatures of the various states but enjoys constitutional recognition as a level of government⁴⁹.

By the 73rd Amendment Act, besides the center and state levels, Panchayats at and below the district level emerge as the third stratum of government. For, 'unlike the past attempts of revamping the Panchayats more as efficient delivery outlets, there has been a fundamental attitudinal change to make the Panchayats genuine institutions of self-government

⁴⁷Khan, R, op.cit. p.64

⁴⁸GoI, '*Agenda for State Ministers Conference on Panchayati Raj*', Ministry of Rural Development, 2001, New Delhi, p.7

⁴⁹Arora, B, '*Adapting Federalism to India: Multi-level and Asymmetrical Innovation*', in Arora, B and Verney, D, ed., '*Multiple Identities in a Single State, Indian Federalism in Comparative Perspective*', Konark, New Delhi, 1995, p.89

as an alternative to the existing bureaucratic district administration'⁵⁰. However PRI's do not enjoy the powers of a government as they are not assigned any police powers. They are mainly local level institutions comprising of elected representatives to identify, formulate, implement and monitor development and welfare programs. Accordingly the State governments are required to pass necessary legislation to create PRI's and endow them with such financial powers and functional responsibility as they deem appropriate. Thus while the Constitution visualizes Panchayats as institutions of self-governance, however, giving due consideration to the federal structure of our polities, most of the financial powers and authorities to be endowed on Panchayats have been left at the discretion of concerned state legislature. Consequently the powers and functions vested in PRI's vary from state to state.

Article 243(H) recognizes Panchayats as 'institutions of self-government' with prime responsibility of promoting economic development and ensuring social justice. It provides for a fully elected structure at three levels-village, district and an intermediate level. Substantial changes did take place in at least three fronts.

First, certainty of panchayat institutions has been assured. Every state has to establish Panchayats. Their space in the institutional structure of Indian State is now guaranteed.

Second, continuity of the institutions through elections every five years has been stipulated.

Third, entry of weaker sections of people including women in the power structure of Panchayats has been provided. Today, Panchayats elect three million members of whom one million are women and 0.66 million belong to the Scheduled Castes\Scheduled Tribe communities. As many as 175 district Panchayats, 1970 intermediate Panchayats and over 77,000 village Panchayats are headed by women. Positioning of

⁵⁰Bandhopadhyaya, D, '*Peoples Participation in Planning- Kerala Experiment*', Economic and Political Weekly, September 27,1997, p.2450

innumerable elected bodies below the state level, within them of the people belonging to the weaker sections, constitute an event that cannot be dismissed easily⁵¹.

There are provisions for election by an independent State Election Commission in each state, regular election at the end of five year period, reservation of membership and chairperson's position for weaker sections of SC\ST and women, indicative list of subjects in social sectors for devolution of responsibility and function to these institutions by each state and above all the provision for a State Finance Commission in each state to suggest devolution\transfer of tax\non-tax revenues. Finance is accepted as the lifeblood of institutions like PRI, which have been entrusted with the task of socio-economic development of the community. To the extent the sources of revenue are local, authority gains independence⁵².

With such a blueprint, the Amendment has been hailed as a revolutionary step towards establishing a guarantee for people's participation and self-governance. Now besides the center and state levels, Panchayats at and below the district level emerge as the third stratum of government. Two fundamental changes have come about in Indian democratic polity.

Firstly, the democratic base of the Indian polity has widened. (See Table-1.1). Secondly, these amendments are bringing about significant changes in Indian federalism⁵³.

India is on the move to become a multi-level federation. Although the elected bodies have no legislative powers and de jure the union and states constitute the federal India, the qualitative change that has come

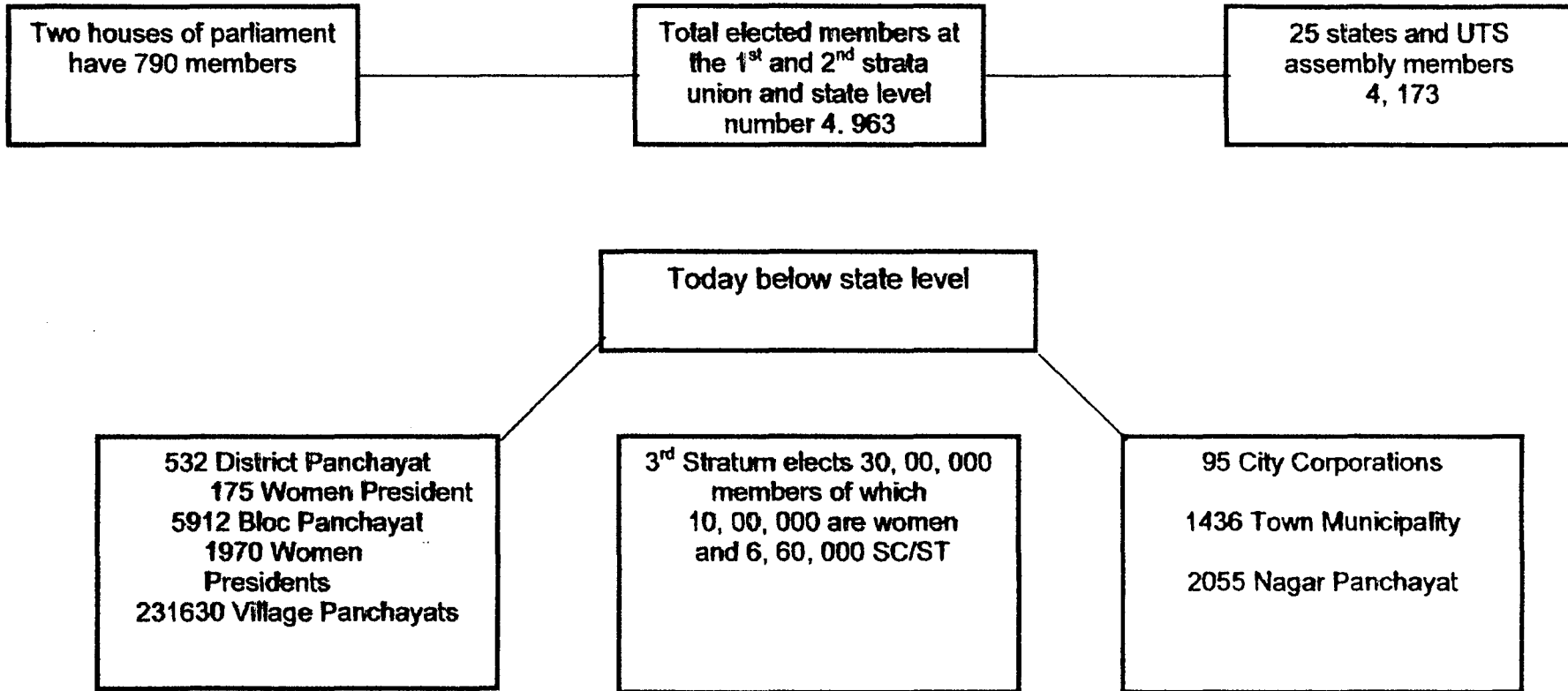
⁵¹ NCRWC, 'A Consultation Paper on Review of the Working of the Constitutional Provisions for Decentralization', ncrwc@nic.in.com, para.1.2

⁵² Singh, RVP, 'Financing of PRI's', Deep and Deep Publication, New Delhi, 1993, p.43

⁵³ Mathew, G, 'Panchayati Raj in India', op.cit., p.10

Table-1.1

INCREASED DEMOCRATIC BASE OF THE INDIAN POLITY AFTER 1993



Source: ISS, Status of PR in States & UT of India, 2000

about in the Indian federal structure has far reaching consequences. The village council \ Panchayat is not new in India. They existed in tradition and were created later by statutes in different provinces and states as the subject is within their competence. They are responsible for development and welfare programme delivery. What is new however is their universality, constitutionally mandated and fully elected structure at three levels- village, district and an intermediate level. The 73rd Amendment may be regarded as the stepping stone in evolving a multi-level federal structure. These provisions combine representative and direct democracy into a synergy and are expected to result in an extension and deepening of democracy in India. Hence Panchayats have journeyed from an institution within the culture of India to attain constitutional status.

CHAPTER 2

PANCHAYATI RAJ INSTITUTIONS– SOURCES OF FINANCE

The 73rd Constitution Amendment Act, 1992, provided the much needed opportunity for the local people to be an integral part of the planning and development process of their village. This decentralization of powers, it is hoped would promote¹-

- Efficiency as the decision makers are local people who know about the local conditions and hence bring about optimum utilization of funds.
- Accountability as decision makers who live in the same locality are under close scrutiny by the villagers.
- Sustainability as Panchayats and Gram Sabhas are constitutionally mandated bodies, regular elections and flow of funds are assured etc.

Financial independence is a prerequisite for autonomy of any institution. It is all the more true of Panchayats, if they have to become institutions of governance at the district level and below. The Panchayats in the pre-1992 period did not enjoy any taxing power or any exclusive domain under the Constitution of India. The State governments, out of the tax powers allocated to them under the seventh schedule assigned taxes to the Panchayati Raj Institutions. Over the years this practice created a 'piquant situation in which Panchayats feel accountable to the state and not to the people for whom they are meant for'². It is undoubtedly true that 'Panchayat finance' was among the major reasons attributed to the failure of the Panchayats during the 1960s and 1970s. The various committees and commissions that were appointed in the past have

¹ PRIA, '*Strengthening Panchayati Raj Institutions: Awareness, Capacity Building and Devolution*', New Delhi, 2001, Pp.18-19

² Rajiv Gandhi Foundation (RGF), '*Dialogue on Panchayats*', New Delhi, 1999, p.4

generally concluded that adequate finances are not available for performing functions allotted to Panchayats.

Under the 73rd Amendment Act 1992, the Panchayats are required to be endowed with adequate responsibilities, powers and finances to enable them to function as the 'institutions of self-government'. Transfer of funds to lower levels of government can be justified on the basis that such transfers can help equalize income distribution throughout the country by reducing inter-regional service and income difference.

For this they must have adequate fiscal capacity as well as substantial fiscal autonomy. The fiscal capacity may be defined as the capability of the Panchayat to raise financial resources commensurate with the functions assigned to it. In other words, the functions assigned to a Panchayat institution must match with the financial resources it is capable of raising from various sources including grants from the State government. Fiscal autonomy, on the other hand, is the extent of independence the Panchayat has in raising and spending financial resources. This means that its dependence on the discretionary funding from the higher level government for the discharge of its 'core functions' should be minimum, and on the other hand, it should not be unduly bound by the conditionalities of 'tied' grants coming from the State Government³. Financial autonomy implies vesting of financial powers in Panchayats to spend funds without taking technical permission and approval of district authorities or Block Development Officer.

POST 1992

In order to resolve the financial problems of the Panchayats provisions were made under Article 243 by the 73rd Amendment Act

³ NCRWC, '*A Consultation Paper on Review of the Working of the Constitutional Provisions for Decentralization*', ncrwc@ nic.in.com, para-4.1

1992. The State governments are expected to devolve powers upon Panchayats to make them fully functional. State legislatures have been vested with powers to make laws regarding the devolution of powers upon Panchayats. Without adequate funds and financial autonomy Panchayats will not be able to function as institutions of self-government.

Article 243-G of the Constitution of India, which deals with the crucial issue of powers, authority and responsibilities of the Panchayats, states that a State legislature, by law, may provide such provisions for the devolution of powers and responsibilities upon the Panchayats with respect to-

- Preparation of plans for economic development and social justice
- The implementation of such schemes for economic development and social justice as maybe entrusted to them including those in relation to the ones listed in the 11th Schedule⁴. (Refer Annexure-1)

'Devolution' in the context of the Panchayats, means that when the authority in respect of a specific activity is transferred from the state to the local governments, the latter should have the prerogative of taking decisions in respect of planning and implementation of such activity⁵.

Article 243-H provides the 'powers to impose taxes by and funds of, the Panchayats- the legislature of a state may, by law, -

- Authorize a Panchayat to levy, collect and appropriate such taxes, duties, tolls and fees in accordance with such procedures and subject to such limits;
- Assign to a Panchayat such taxes, duties, tolls and fees levied and collected by the state government for such purposes and subject to such conditions and limits;

⁴ Government of India (GoI), 'Agenda for State Ministers Conference on Panchayati Raj', Ministry of Rural Development, July 2001, p.8

⁵ GoI, 'Report on the Task Force on Devolution of Powers and Functions upon Panchayati Raj Institutions', Ministry of Rural Development, 2001, p.5



- Provide for the making of such grants-in-aid to the Panchayats from the consolidated fund of the state; and
- Provide for constitution of such funds for crediting all moneys received, respectively, by or on behalf of the Panchayat and also for the withdrawal of such moneys, there from as maybe specified in the law⁶.

SOURCES OF FUNDS FOR PRIs

For carrying out their functions the finances of the Panchayat are generally drawn from the following-

TAX ASSIGNMENT

Local tax authority is a legislative authorization of tax power delegated by the state government to a local body. The purpose of such assignment of tax powers and authority to the PRI is to encourage them to shoulder their fiscal responsibility to place them in a position to raise their own resources and thereby reduce their dependence on revenue grants from the state. Self-sufficiency and fiscal autonomy of the Panchayats presupposes that the states should assign some of the buoyant and income elastic sources to the three levels of Panchayats. The general principle that guides the division of fiscal powers is that the local government should be assigned those taxes whose burdens are likely to be locally absorbed i.e. which are not easily exportable to residents who do not benefit from the local services that are being financed by the revenue rose.

According to the State Panchayats Acts, there are a number of taxes levied at different levels of the Panchayats. With the exception of some states most of the Panchayats Acts does not make any distinction

⁶ Bakshi, PM, '*The Constitution of India*', Universal Law Publication, New Delhi, 1998, p.184

between obligatory and optional levy. There are no floor rates fixed⁷. The Panchayats at the lowest level are generally empowered to levy taxes, fees and charges. The first and second tier, which is Zilla Parishad and Panchayati Samiti are not entrusted with the taxing power. Even if the power of levying taxes, fees and charges is entrusted to the Zilla Parishad or block level, they are mostly collected at the village level and passed on to the upper tiers of the Panchayati Raj institutions. The Gram Panchayats is limited in space and their proximity to the people and the area to be served by them is both direct and close. These layers of local government are ideally suited to perform such functions as a mostly civic and welfaristic in nature and whose benefits are internalized to a great extent. This maybe the precise reason why most of the revenue powers and civic responsibilities are entrusted to these units⁸. Therefore tax assignment and tax sharing are discussed with respect to village Panchayats only.

The Gram Panchayat are entrusted with the power to levy a number of taxes, the most important among them are⁹-

- (i) Land tax (non-agricultural)
- (ii) House/ building tax
- (iii) Vehicle tax
- (iv) Tax on profession, trade and calling
- (v) Tax on fairs and other entertainments
- (vi) Tax on advertisements
- (vii) Octroi on animals or goods or both brought for sale
- (viii) Lump sum levy on factories in lieu of taxes
- (ix) Special taxes for construction and public work

⁷RGF, '*Revitalization of Panchayati Raj in India*', New Delhi, 1997, p.20

⁸Subrahmanyam, K Siva, '*Functional and Financial Devolution on PRIs, a Study in Andhra Pradesh*', NIRD, Hyderabad, 1999, p.1

⁹RGF, '*Revitalization of*', op.cit. p.21

Rajiv Gandhi Foundation in its report of the Task Force on PRI carried a study of fourteen State Conformity Acts- Andhra Pradesh, Bihar, Gujarat, Haryana, Himachal Pradesh, Karnataka, Kerala, Madhya Pradesh, Maharashtra, Punjab, Rajasthan, Tamil Nadu, Uttar Pradesh and West Bengal. Of the 14 major states, 8 states levy land tax on agricultural land. Similarly, with the exception of Bihar and UP, tax on house and building is common in all the states. The third important tax is on non-motorized vehicles. Amongst the 14 states it is commonly levied in 11 states, but it is not an optional levy. Another important tax is on profession, trade and callings, which is levied in 9 states. The states of HP, MP and Punjab have an obligatory levy. The tax on fairs and other entertainments though levied in 7 states is found obligatory in Kerala, Punjab and West Bengal. Tax on advertisement is levied in only 3 states of Andhra Pradesh (obligatory), Karnataka and Kerala. The Gram Panchayat in Gujarat, Maharashtra and Rajasthan levy octroi on goods and animals. Another tax levied frequently across the states is a special tax on construction of public works. A betterment levy is found only in Maharashtra¹⁰.

NON-TAX REVENUE

In addition there are fees and charges (user charges) levied by the village Panchayat for the provision of public facilities¹¹:

- (i) Water rate
- (ii) Lightning fee/rate
- (iii) Street clearing fee
- (iv) Conservancy fee
- (v) Drainage fee
- (vi) Sanitary fee for public toilets
- (vii) Pilgrimage fee

¹⁰ Ibid.

¹¹ Ibid.

Village Panchayats also levy some kind of fee for the use of common resources like –

- (i) Fee for the use of Panchayat shelter
- (ii) User charge for hospitals and schools
- (iii) Fee for use of common grazing land etc.
- (iv) Fee on markets and weekly bazaars
- (v) Fees on animals sold

For the Gram Panchayats, the first important instrument to raise revenue is to levy taxes. Of the fourteen states, about eight levy the land tax on non-agricultural land. Similarly, with the exception of Bihar and Uttar Pradesh, the tax on houses and buildings is common in all the states. The other important tax is the tax on non-motorized vehicles. Of the fourteen it is commonly levied in eleven states, but it is an optional levy. Tax on profession, trade and callings is levied in nine states of which in the states of Himachal Pradesh, Madhya Pradesh and Punjab this is an obligatory levy. In Bihar and Uttar Pradesh, this is treated as income-based levy. The tax on fairs and other entertainments, though levied in seven states, is found in Kerala, Punjab and West Bengal. Tax on advertisements is levied only in three states of Andhra Pradesh (obligatory), Karnataka and Kerala. The Gram Panchayat in Gujarat, Maharashtra and Rajasthan levy octroi on goods and animals. Another tax levied frequently across the states is a special tax on construction of public works. It is generally levied on the adult male members of the household and commutable into a labour contribution. A betterment levy is found in Maharashtra¹².

The second important instrument of raising resources at the Gram Panchayat level is to charge fees for using public facilities and common resources. The water rate and lighting fees for the maintenance of street lighting and water supply is levied in 13 and 10 states respectively. The village Panchayats in Andhra Pradesh do not levy water fee, whereas in

¹² Ibid. p.21

Tamil Nadu it is collected along with the land revenue. In Kerala it is an obligatory levy. Only Kerala and Madhya Pradesh have fees for the maintenance of streetlights. Some of the states like Andhra Pradesh, Karnataka, Rajasthan and Tamil Nadu do not charge for this facility. For the maintenance of cleanliness in villages there are street cleaning fees in Andhra Pradesh, Haryana, Himachal Pradesh and Uttar Pradesh. A drainage fee is levied in Kerala, Madhya Pradesh and Rajasthan. There are 8 states, which levy a conservancy fee, which in Kerala and Madhya Pradesh is obligatory. The user charges on hospital and schools are levied in Bihar, Rajasthan and Madhya Pradesh. For providing sanitary facilities to the pilgrims, 7 states levy a kind of pilgrim tax. For the use of common resources like grazing land, ponds etc., the Gram Panchayats of 7 states levy a fee whereas 11 levy a fee for use of Panchayat shelters with the exception of Haryana and Himachal Pradesh which do not charge either of the fees. Another important fee which is levied in 10 of the states is the levy on markets and weekly bazaars. The Gram Panchayats in Andhra Pradesh collect a fee on the village produce while in Rajasthan it is charged on commercial crops brought for sale in the markets. The other kinds of fees, though less common, are on animals sold and a lump sum levy on factories in lieu of taxes¹³.

SHARED TAXES

Tax sharing is the second important instrument of resource mobilization at the Panchayati Raj level. Taxes which are assigned by statute to PRIs but are collected by state government and then revenue being passed to Panchayats are called assigned taxes. Shared taxes are those assigned to state government and collected by them but share of their proceeds go to local bodies¹⁴. The purest form of shared tax = type A grants requires that some proportion of the amount collected in the

¹³ Ibid.

¹⁴ PRIA and NCROs, *Status of Finances of Panchayati Raj Institutions- an Overview*, New Delhi, 1999, p.10

jurisdiction of a local government be returned to that local government i.e. that a derivation principle of revenue sharing be applied. The higher level deducts a fee for collection, usually a specified percentage of total receipts. Under this system, the local government has no control over determination of rate and base. Type A is thus an inter-governmental transfer and not local tax. Land revenue and stamp duties are the two most important taxes, which are in the shared fiscal domain of the state government and the Panchayats.

The basis of the levy of land revenue is agricultural land and the stamp duty is levied on the transfer of properties¹⁵. The major tax base of the rural areas, that is, agricultural land, are tapped by the states leaving non-agricultural land and rural houses and buildings to the fiscal domain of the PRI's. Land revenue is commonly shared with PRI's across the states, even in respect of basic levy, with the exception of Haryana. In 5 states (Gujarat, Karnataka, Kerala, Maharashtra and Punjab) land revenue is shared on the basis of the origin of the collection while in the remaining states the levy is shared by a formula. The shared basic levy is passed to one or more of the three tiers of PRI's. Exceptionally the land revenue is not levied in Haryana. Stamp duty is also a buoyant source of revenue for most of the states as compared to land revenue, which contributes a little over one percent of aggregate revenue of state governments. In case of stamp duty, it is shared only in respect of addition to basic levy. Under the present legislation, the basic levy is not shared with the PRI's. With the exception of Bihar, Gujarat, Rajasthan and UP the additional stamp duty is not shared in the remaining ten states. In most of the states there is an additional stamp duty between 1 to 5% from which revenue is assigned to Panchayats. Gujarat and Rajasthan empower village Panchayats to levy local surcharge instead at rates

¹⁵ Bohra, OP, '*Financial Resources of Panchayats in India*', in Konrad Adenauer Foundation, '*National Conference on Emerging Trends in Indian Local Government Finances, October 1996*', Manohar, New Delhi, 19998, p.85

tapped at some percentage of the basic levy. Locally levied surcharges are retained locally whereas the revenue from additional duty is distributed more often by formula than by origin¹⁶.

In addition to the above two sources of revenue there are other sources like¹⁷ –

**Seigniorage* (royalties) – collected by the state government on minor minerals and quarried materials like granite and sand that are shared with the Gram Panchayats in some states like Andhra Pradesh, Maharashtra and Tamil Nadu.

**Forest revenue*- the revenue from forest areas collected by the state government is basically a part of the PRIs fiscal domain.

**Other taxes*- the powers to levy entertainment taxes are generally assigned to the Panchayats in most of the states. In Tamil Nadu the entertainment tax is shared on the basis of a formula while in West Bengal the basis of sharing is by origin:

GRANTS-IN-AID

The use of inter-governmental transfers (grants-in-aid) becomes a prominent feature of fiscal institutions in countries with a federal set up. It would be necessary to supplement the finances of the PRIs. It is through such mechanisms that the vertical imbalance and horizontal imbalance can be corrected in a federal polity. The former refers to the mismatch between the revenue earning power and functional responsibilities of a unit of government and the latter refers to the unequal development of areas falling under the jurisdiction of different governmental units. Accordingly, these provisions provide to the States 'a unique opportunity

¹⁶ RGF, '*Revitalization of*', op. cit. p.23

¹⁷ Ibid. p.24

to redesign the existing fiscal system that is coherent and flexible enough to meet the rapidly changing local needs and responsibilities'¹⁸.

Two important objectives of the sub-state level grant system are¹⁹ -

- 1) To serve as an instrument to promote territorial equity, rural-urban as well intra-rural,
- 2) To ensure a basic minimum of public services such as primary education and primary health care.

Broadly, grants can be grouped into two categories (Refer Table-2.1)-

- 1) Conditional (specific purpose) grants
- 2) Unconditional (general purpose) grants

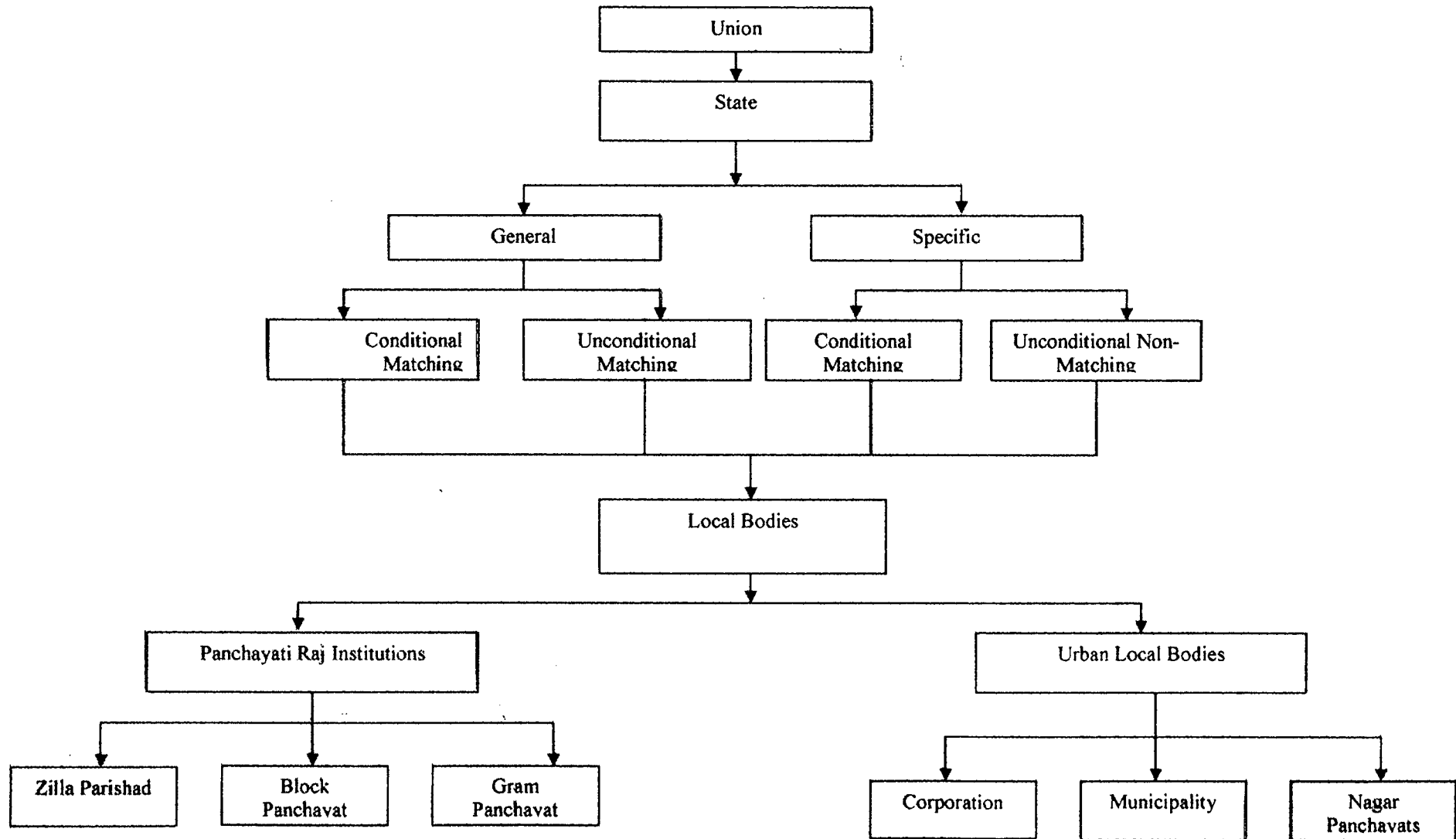
In conditional grants there is a condition attached to them to ensure that apart from spending the amount for the purpose for which it was given, a certain standard has also to be maintained certain percentage of locally financed expenditure maybe assigned to a given service or a specific need. In contrast, in general purpose grants no such conditions are attached. Local bodies can use the grants according to their own local priorities. Generally, the grants are given to the poor or financially weak local bodies to uplift the standard of services provided by them. For every specific purpose (conditional) grant, there is a 'matching grant'. According to a specified formula, the local bodies are reacquired to match each grant rupee or a certain portion of funds they accept with their own revenue. Thus, it becomes obligatory for the local bodies to raise revenue equivalent to the specific purpose grant they get.

There are other type of grants viz. block grants, establishment grants, road maintenance grants, minor irrigation grants and

¹⁸ Mathur, OP, 'State-Local Fiscal Relations', in Srivastava, DK, ed., 'Fiscal Federalism in India: Contemporary Challenges', NIPFP, New Delhi, 2000, p.360

¹⁹Oommen, MA, 'State-Local Fiscal Relations in India. A Search for Analytical Framework', in Konrad Adenauer Foundation, 'National Conference on Emerging Trends in Indian Local Government Finances, October, 1996', Manohar, New Delhi, 1998, p.8

Table-2.1
Taxonomy of Grant Transfers



Source: Oommen, MA, 'State - Local Fiscal Relations in India', in Konrad Adenauer, 'State Local Fiscal Relations in India. October 1996'. Manohar. New Delhi. P - 46

miscellaneous grants. The block grants, which constitute the major proportion of total grants, are given to the PRI's for the execution of public works programs on the basis of applications received from them stating their requirements. The quantum of the grants depends on the type of the projects proposed by the Panchayats²⁰.

Provisions of Grants-in-aid to Panchayati Raj Institutions²¹-

Zilla Parishad

In about 10 states (other than Gujarat, Haryana, Himachal Pradesh, Kerala and Orissa) there is a provision for grants from the center and the states to PRIs. In Bihar and Punjab, there is also a provision for grants from local authorities. In the case of Andhra Pradesh and Orissa, there is provision for grants from all India bodies and institutions for the development of cottage, village and small-scale industries etc. Based on population, in Andhra Pradesh there is also that the government shall make an actual grant at the rate of Rs.5 per person residing in the district. In Gujarat, there are three types of grants – special grants in accordance with the rules, grants of 2% of forest revenue (in Maharashtra this is 5%) and special grants to backward districts. In Haryana, there is a provision of 5%-10% of the funds to be allotted to districts as grants-in-aid by the government under the plan scheme for development and Panchayat departments. In Kerala, there is a provision for discretionary grants. In the states of Karnataka, Maharashtra and TN, the establishment grants to cover the expenses of establishment is provided for. Maharashtra also has the provision of - purposive grant per annum by the state, grants for plan scheme, incentive grants and district equalization grant to obliterate inter district disparities in economic development.

²⁰ RGF, '*Revitalization of*', op.cit. p.25

²¹ Ibid. Pp.27-28

Block Level

In 8 major states there is also a provision of grants at the block level from the center and the state governments (also on the recommendations of SFC). In West Bengal and Karnataka, the grants from Zilla Panchayats and local authorities are also provided for. Based on population, an annual grant of Rs.5 per person residing in the block is provided in Andhra Pradesh. Haryana has a provision of grants for the implementation of community development and rural development programs. Discretionary grants and establishment grants to cover the expenses of establishment are provided in Karnataka. Maharashtra provides local cess matching grants besides the above which are considered surcharge. TN has provision for grants like local education, cess grants and local road grants. In Orissa, like Tamil Nadu, there is also a provision for getting grants from any organization or statutory body.

Village Panchayat level

At the Gram Panchayat (GP) level, the grants from government, Zilla Parishad, Mandal Parishad and \ or other government authorities (also at the recommendation of the SFC) are found most commonly across major states. In addition, Gujarat provides forest revenue grant in select GP and special grants to backward Panchayats. A kind of discretionary grant and an annual grant of Rs. 1 Lakh to every GP (for maintenance of electricity, water supply, sanitation and other welfare measures) are provided in Karnataka. In Kerala there is a provision for basic tax grants, project grants, specific purpose grants and grants from institutions or individuals. Maharashtra provides a grant of a sum equal to an average amount of land revenue and equalization from ZP for reducing disparities in the economic development of the GP. Orissa has the provision of receiving grants from any source. TN is the only state, which provides village house tax matching grant for every rupee of house tax collected.

Central funds-

In many cases they are in the form of programs like Jawahar Rozgar Yojna (JRY). JRY is one of the central grants, which is available to almost all the Panchayats at village and block level. The program is implemented in all states and is funded by the center and the state on 80:20 basis. The number of central funds available with a particular tier of Panchayats varies from state to state²².

ARTICLE 243 I

Consistent with their new role as institutions of self-government, the flow of funds to Panchayats should be adequate to enable them to function effectively. The 73rd Amendment Act has significantly altered the position in the area of the State- Panchayats fiscal relations under Article 243-I and Article 280 of the Indian constitution. Accordingly the mechanism of State Finance Commissions at the state level and the Central Finance Commission is provided with mandatory functions not only to improve the finances of the Panchayats but also to make them an integral part of both the state and the union government finances²³. The basic task of any finance commission consists of designing constitutionally relevant and contextually meaningful transfer arrangements that the terms of reference set out the task for each commission.

The 73rd Amendment Act provides for supplementation of the resources of the Panchayat through the mechanisms of Central Finance Commission under Article 280. The Tenth Finance Commission was not governed by sub clauses 280(bb) and 280(cc) of the Constitution (added subsequent to its appointment in June 1992). So, under Article 275 of the

²²PRIA and NCROs, op.cit. p.16

²³GoI, '*Report of the Task Force on Devolution of Powers and Functions upon PRI's*', Ministry of Rural Development, 2001, p.28

Constitution it made adhoc grants amounting to Rs. 4380.93 Cores for the period 1996-2000 for Panchayats in rural areas²⁴. These grants are in the nature of additionally over and above the amounts flowing to Panchayats by way of taxes, charges and government grants. The commission recommended a grant of Rs.100 per capita as given in the 1971 census, for the Panchayats for its award period. The grant was to be given in addition to the amounts transferred to the Panchayats as shares of assigned taxes, duties, tolls, fees grants-in-aid and activity related budgetary transfers. The local bodies were required to prepare suitable schemes and provide matching contributions. No amount was to be used for expenditure on salaries and wages.

The Eleventh Finance Commission 2000, was mandated to make recommendations for local bodies as per Article 280(bb) inserted by the 73rd Amendment. Article 280(bb) provides that, 'the measures needed to augment the consolidated fund of a state to supplement the resources of the Panchayats in the state on the basis of To recommendations made by the Finance Commission of the State'²⁵. It is for the first time that a presidential order had asked the finance commission to make recommendations on the local bodies based on the recommendations of the State Finance Commission. As per the Terms of Reference NO.6 and the constitutional obligation vested in it by article 280 (3) (bb & c), the Eleventh Finance Commission has in keeping with the availability of resources and the overall limits set for the flow of resources from the center to the states, recommended a total grant of Rs.1, 600 crores for the Panchayats each of the five years starting from the financial year 2000-2001. They are meant to be spent on three items viz. maintenance of accounts, creation of database relating to local finance and maintenance

²⁴ Rai, M, M Nambiar, S Paul, S V Singh and S Sahni, ed. '*The State of Panchayats-a Participatory Perspective*', PRIA\ Samskriti, New Delhi, 2002, p.156

²⁵ GoI, '*Report of the Task Force on Devolution of Powers and Functions upon PRI'S*', Ministry of Rural Development, 2001, p.9

of civic services. This amount unlike the Tenth finance commission which adopted population as the sole criterion for allocation of adhoc grants to the states, shall be provided by Eleventh Finance Commission on the following criteria and weights²⁶:-

(i)	Population	40%
(ii)	Index of decentralization	20%
(iii)	Distance from highest per capita income	20%
(iv)	Revenue effort	10%
(v)	Geographical area	10%

On the basis of an elaborate methodology, an index of decentralization was constructed on the following ten parameters²⁷:

- (i) Enactment of State Panchayat legislation in conformity with the 73rd Constitution Amendment Act;
- (ii) Intervention restriction in the functioning of the Panchayats;
- (iii) Assignment of functions to the Panchayats in the State Panchayats legislation vis-a-vis the 11th schedule;
- (iv) Transfer of functions to the Panchayats by the way of rules
Notifications orders of state government;
- (v) Assignment of taxation powers to the village Panchayats as per State Panchayat Acts;
- (vi) Levy of taxes by the village Panchayats;
- (vii) Constitution of SFC and submission of action taken reports;
- (viii) Action taken on the major recommendations of the SFC;
- (ix) Elections to the Panchayats;
- (x) Constitution of district planning committees.

²⁶GoI, '*Report of Eleventh Finance Commission*', 2000, para-8.27

²⁷ Ibid. para-8.24

This has been done to induce the states to speed up the process of decentralization so that these develop as institutions of self-government as envisaged under Articles 243(D).

By far, the most novel provisions that brought the local government institutions in the scheme of fiscal federalism are contained in Articles 243-I. Unlike the central finance commission whose task is made easy by specifying the scope of fiscal transfers from the center to the states in the shape of transferred taxes, grants and loans, the State Finance Commissions have no past experience of the subject. This is the first time that finance commissions have been appointed to look at the financial resources of the Panchayats. They envisaged the setting up of State Finance Commission as soon as maybe within one year from the commencement of the Constitution (73rd Amendments) Act, 1992 and thereafter after the expiration of every fifth year in every state for reviewing the financial status of the Panchayats and to make recommendations to the governor regarding principles governing the major issues mentioned in Article 243(H) and measures to improve the same by restructuring, if necessary, the state-local fiscal relationship²⁸.

The SFC's, the first ever, in almost all the states have submitted their reports to their respective state government and these have been accepted in their partial or modified form. The status as on 1st July 2000 , with regard to the setting up of SFC's and submission of their report after the coming into effect of Constitutional amendments is provided in Table - 2.2.

It will be seen that the first reports of SFC's have been submitted in all the states (except Bihar) and in some states, second SFC's have been set up. The SFC's first reports have been successful in creating the concept of a divisible pool between the states and the local bodies, almost similar to the pattern of central revenue to the states. The SFC's have

²⁸ NCRWC, op. cit. Para-4.16

Table 2.2

Status of State Finance Commissions (as on 1 July 2000)

State/Union Territory	First State Finance Commission			Second SFC Constituted on
	Constituted on	Report Submitted on	Action Taken #	
Andhra Pradesh	June 22, 1994	May 31, 1997	4	Dec. 8, 1998
Arunachal Pradesh	SFC not constituted as the State Panchayat Act did not receive assent of the President			
Assam	June 23, 1995	Feb. 29, 1996	1	-
Bihar	April 23, 1994	Report not submitted	-	-
Goa	April 22, 1994	June 5, 1999	1	-
Gujarat	Sept. 15, 1994	July 13, 1998	1	-
Haryana	May 31, 1994	March 31, 1997	2	-
Himachal Pradesh	April 23, 1994	Nov. 30, 1996	3	May 25, 1998
Karnataka	June 10, 1994	Jan. 31, 1996 (Urban Local Bodies)/ July 30, 1996 Panchayat Raj Institutions	4	June 23, 1999
Kerala	April 23, 1994	Feb. 29, 1996	3	June 23, 1999
Madhya Pradesh	June 17, 1994	June 20, 1996	4	June 17, 1999
Maharashtra	April 23, 1994	Jan. 31, 1997	4	June 22, 1999
Manipur	April 22, 1994	Dec. 20, 1996	4	-
Orissa	Nov. 21, 1996	Dec. 30, 1998	4	-
Punjab	April 22, 1994	Dec. 31, 1995	2	-
Rajasthan	April 23, 1994	Dec. 30, 1995	3	May 7, 1999
Sikkim	July 22, 1998	Aug. 16, 1999	2	Aug. 16, 1999
Tamil Nadu	April 23, 1994	Nov. 26, 1996	4	Dec. 1, 1999
Tripura	April 23, 1994	Jan. 12, 1996	4	Oct. 29, 1999
Uttar Pradesh	Oct. 22, 1994	Dec. 26, 1996	4	Feb. 25, 2000
West Bengal	May 30, 1994	Nov. 27, 1995	3	-
Pondicherry	March 1997	Sept. 15, 1997*	5	-
Chandigarh	April 1995	De. 31, 1997	1	-
Delhi			1	-
A&N Islands			2	-
D&N Haveli	Sept. 8, 1995	Aug. 28, 1998	2	-
Daman & Diu			2	-
Lakshadweep			2	-

Note: #Action taken: 1 = No action taken; 2 = Report under consideration of the State Government/UT Administration; 3 = Accepted; 4 = Accepted with modifications; 5 = Information not available.

Jammu and Kashmir, Mizoram, Meghalaya and Nagaland are excluded from the purview of the Constitution (Seventy-third Amendment) Act, 1992.

* This was the first report to be followed by a report every six months. The Commission was constituted for three years.

Source: NCRWC, *A Consultation Paper on Review of the Working of the Constitutional Provisions for Decentralization (Panchayats)*

recommended a certain percentage of the net proceeds of the total tax revenue of the state for transfer to the local bodies. In some states, certain taxes have been earmarked; a certain percentage of the proceeds from which could be transferred to the local bodies. Some SFC's have identified innovative parameters for distribution of divisible pool fund among different local bodies in order to ensure horizontal equity²⁹.

The SFC's have been given the task of determining the grants-in-aid from the state to the Panchayats. These grants are expected to accrue to the PRI for a multiplicity of reasons; per capita general purpose grants, for meeting the PRIs non-plan expenditure responsibilities, compensatory grants for specific purpose, for example- for preparation of registers and forms, up gradation of primary health and rural water supply, one-time non-recurring grant, incentive grants, development grant, non-statutory grants and the like.

SIGNIFICANCE of FINANCIAL DEVOLUTION

The devolution package given by the SFC's is marked by significant inter- state variations. These variations relate to³⁰ –

- composition of the divisible pool of state resources
- The proportion in which this pool is to be shared with the Panchayats.

While the state governments recognize the link between the functional responsibilities and funds, few states have considered it essential to follow up on the XI Schedule of the constitution 73rd Amendment Act. The Panchayati Raj Institutions continue to face paucity of funds even after several years since the 73rd Amendment Act has been passed. For self-sufficiency and fiscal autonomy of the Panchayats, it is important that states make a concerted effort to provide them with

²⁹ NIPFP, '*Reports of the Finance Commissions of States-A Preliminary Review*', New Delhi, 2000, p.7

³⁰ RGE, '*Road Blocks to the Institutions of Self-Government*', New Delhi.1999, p.4

adequate financial resources. It has led to the shifting of the entire debate from center-state relationship to the State-Panchayat relationship. For a truly multi-federal structure in India therefore, if resources have to be distributed, the question should not restrict to the central or state government but Panchayats as well which in itself is a three-tier structure.

CHAPTER 3

OBSTACLES IN FINANCING PANCHAYATI RAJ INSTITUTIONS

Constitutional status has been guaranteed to the Panchayats by the 73rd Amendment Act 1992. Despite this achievement, no evidence is yet available to indicate that the country is moving towards a system of decentralized governance with Panchayats as governments at the third stratum capable of voicing the 'local will' and empowered to exercise autonomy over local functions. Those who noticed radical elements in the Constitution Amendment believed that as institutions of self-government nearest to the people, Panchayats would assert their autonomy and prepare the ground for dispersal of political power at an unprecedented scale. But elections have not been held regularly, functional and financial devolution has not taken place, administrative and financial resources have been denied to the Panchayats, Gram Sabhas have not been empowered and even right of Panchayats to prepare development plans and implement them has not been given proper recognition. Besides, both Central and State governments have set up implementation machinery for development schemes by-passing the Panchayats and have been responsible for the creation of parallel power-structures outside the Panchayati Raj system.¹

Though a neat matching of function or expenditure, responsibilities and finance or revenue raising capabilities of the various tiers of government in any federal setup is extremely difficult, some measure of parity is needed besides adequate built-in provision for reviewing and rectifying the possible mismatches. The tragic part is that even under the new dispensation following the 73rd Amendment Act, there has not been much serious effort to maintain some measure of vertical fiscal balance in

¹ NCRWC, '*Consultation Paper on Review of the Working of the Constitutional Provisions for Decentralization*', ncrwc@nic.in.com, para-1.3

the diversion of functions and finance at the union, state and sub-state level. There is infact much ambivalence and mismatch at the PRI level². Finance has been accepted as a life-blood of the institution like PRI, which has been entrusted, with the task of socio-economic development of the community and establishment of autonomous local self-government. Their ability to discharge the functions entrusted to them depends on resources. Obviously they need finance in adequate quantity³. In less than a decade, various studies and reports available point out that the financial autonomy of the PRIs is severely constrained. The 73rd Amendment Act has not made a clear-cut financial provision for the lowest tier as the Constitution had made the center-state relations. Local government continues to be plagued by inadequate finances. This can be attributed to a host of reasons.

FISCAL DECENTRALISATION

NCRWC (2001) in its paper found many shortcomings in the working of the PRIs due to financial constraints. This is reflected in the expenditure decentralization ratio which represents local government expenditure as percentage of State government expenditure. PRI expenditure as percentage of total expenditure of State government is less than 10% in as many as 7 out of 12 states (refer Tble3.1). In 6 states it is less than 5%. Out of the 5 remaining states, expenditure decentralization ratio in respect of PRIs is between 11%-20% in 4 states. The State of Karnataka only is found to be an exception where local government expenditure constitutes more than 30% of the state expenditure⁴. NCRWC also looked into tax-revenue decentralization ratio, which indicates percentage of local government tax revenue to total state government tax revenue. It was found that out of 12 major states, the tax

² NCRWC.op.cit. para-3.11

³ Singh, RVP, '*Financing of Panchayati Raj Institutions*', Deep and Deep, New Delhi, 1993, p.45

⁴ NCRWC, op.cit. para-4.3

Table 3.1**Expenditure Decentralization Ratio**

Figures in Rs. Lakhs

States	Total Expenditure PRIs 1997-98	Total Expenditure ULBs 1997-98	Total Expenditure (ULBs+PRIs)	State Total Expenditure (RE) 1997-98	PRIs Expenditure as % of Total State Exp.	ULBs Expenditure as % of Total State Exp.	Local Govt. Exp. as % of State Exp.
Assam	4056.91	5338.47	9395.38	475939.00	0.85	1.12	1.97
Gujarat	226880.85	95089.25	321970.10	1155902.00	19.63	8.23	27.85
Haryana	14642.90	34425.57	49068.47	634809.00	2.31	5.42	7.73
Karnataka	369640.89	44585.38	414226.27	1183320.00	31.24	3.77	35.01
Kerala	73056.08	27261.64	100317.72	920388.00	7.94	2.96	10.90
Madhya Pradesh	178529.90	62143.64	240673.54	1222886.00	14.60	5.08	19.68
Orissa	64002.25	13787.79	77790.04	582310.00	10.99	2.37	13.36
Punjab	15954.89	35939.89	51894.78	819565.00	1.95	4.39	6.33
Rajasthan	153738.30	48902.45	202640.75	920972.00	16.69	5.31	22.00
Tamil Nadu	49061.87	125191.9	174253.77	1489359.00	3.29	8.41	11.70
Uttar Pradesh	90714.07	60587.18	151301.25	2509649.00	3.61	2.41	6.03
West Bengal	55487.91	38111.55	93599.46	1269906.00	4.37	3.00	7.37

Source: NCRWC, A Consultation Paper on Review of the Working of the Constitutional Provisions for Decentralization (Panchayats)

revenue of local bodies in 6 states constituted less than 5% of the total tax revenue of the state (refer Table-3.2)⁵. This indicates that the local bodies have not been given sufficient tax assignments to raise revenue locally.

In terms of revenue collected by the Gram Panchayats it was found by NCRWC that in 6 states out of 12 major states, GP collected less than 10% of their revenue requirements (Refer Table-3.3). When all the three tiers of Panchayats are taken into account, the position deteriorates further. The position of Gujarat, Haryana, Punjab, Kerala, Karnataka and Assam is much better⁶.

Also the capacities of PRIs to meet their revenue expenses from own sources are weak. In 8 out of 12 major states, the GPs can meet not more than 12% of their revenue expenditure from internal sources. An immediate impact of this is the lack of autonomy of the PRIs to finance from its own funds; the maintenance expenses of the core services that is water supply, street lighting, sanitation and roads. Expenditure on the core services as a percentage of total revenue expenditure is low in all the states and below even 1% in a number of states. Similarly, very small portion of internally collected revenue is spent on core services. Local governments own revenue receipts constitute an infinitesimal proportion of the total government revenues.

Grants-in-aid constitute the major prop on which the entire edifice of the Panchayats rests. Obviously without these revenue transfers, the very existence of the Panchayats comes to a halt. Except in big and prosperous Gram Panchayats, grants-in-aid account for about 80% of the total receipts of the Panchayats at all levels. The system of grants is yet not rationalized; despite the first generation SFC's having completed their tasks. There is no integrated system of grants in several states. The existing system does not satisfy the principles of predictability or certainty

⁵ NCRWC, *op. cit.* para-4.7

⁶ *Ibid.* para-4.5

Table 3.2
Revenue of PRI's

<i>Figures in Rs. Lakhs</i>						
States	Own Revenue		Total Revenue		Own revenue as % of Total Revenue	
	GP	PRIs	GP	PRIs	GP	PRIs
Assam	234.85	345.99	1391.85	1550.31	16.87	22.32
Gujarat	3158.25	4036.11	9838.40	223253.71	32.10	1.81
Haryana	5295.00	5301.00	7744.00	8522.00	68.38	62.20
Karnataka	3013.72	3013.72	23365.29	376806.54	12.90	0.80
Kerala	9909.34	9909.34	74427.39	98276.59	13.31	10.08
Madhya Pradesh	2718.24	3203.83	68242.67	177901.47	3.98	1.80
Orissa	699.38	699.38	14573.15	64002.25	4.80	1.09
Punjab	4610.30	5386.62	10117.51	13541.04	45.57	39.78
Rajasthan	1344.00	3074.57	80109.82	152020.75	1.68	2.02
Tamil Nadu	2575.30	3403.77	27929.04	42216.41	9.22	8.06
Uttar Pradesh	382.13	4665.17	73281.22	88324.36	0.52	5.28
West Bengal	1296.51	1959.21	25507.46	48775.46	5.08	4.02

Source: NCRWC, A Consultation Paper on Review of the Working of the Constitutional Provisions for Decentralization (Panchayats)

Table 3.3

Revenue Receipts and Expenditure of PRIs : 1997-98

States	Own Revenue		Total Expenditure		Expenditure on Core Services		Own revenue as % of Total Expenditure		Expenditure on Core Services as % of Own Revenue		Expenditure on Core services as % of Total Expenditure	
	GP	PRIs	GP	PRIs	GP	PRIs	GP	PRIs	GP	PRIs	GP	PRIs
	Figures in Rs. Lakhs											
Assam	234.85	345.99	2919.69	4056.91	1049.68	1082.14	8.04	8.53	446.96	312.77	35.95	26.67
Gujarat	3158.25	4036.11	5908.53	226880.85	1657.28	1657.28	53.45	1.78	52.47	41.06	28.05	0.73
Haryana	5295.00	5301.00	13652.00	14642.90	NA	NA	38.79	36.20	NA	NA	NA	NA
Karnataka	3013.72	3013.72	24365.02	369640.89	5727.05	36124.04	12.37	0.82	190.03	1198.65	23.51	9.77
Kerala	9909.34	9909.34	44057.89	73056.08	7191.05	8725.05	22.49	13.56	72.57	88.05	16.32	11.94
Madhya Pradesh	2718.24	3203.83	70767.86	178529.90	2563.73	5640.33	3.84	1.79	94.32	176.05	3.62	3.16
Orissa	699.38	699.38	14573.15	64002.25	436.63	793.25	4.80	1.09	62.43	113.42	3.00	1.24
Punjab	4610.30	5386.62	12382.88	15954.89	3910.10	3915.10	37.23	33.76	84.81	72.68	31.58	24.54
Rajasthan	1344.00	3074.57	82123.69	153738.30	NA	1163.57	1.64	2.00	NA	37.84	NA	0.76
Tamil Nadu	2575.30	3403.77	23753.93	49061.87	10832.00	16386.42	10.84	6.94	420.61	481.42	45.60	33.40
Uttar Pradesh	382.13	4665.17	74361.98	90714.07	5060.44	5060.44	0.51	5.14	1324.27	108.47	6.81	5.58
West Bengal	1296.51	1959.21	31515.93	55487.91	63.00	194.51	4.11	3.53	4.86	9.93	0.20	0.35
<p><i>Source: NCRWC, A Consultation Paper on Review of the Working of the Constitutional Provisions for Decentralization (Panchayats)</i></p> <p>N.B. Core Services mean water supply, street lighting, sanitation and roads.</p>												

as the financial fortunes of the Panchayats are made contingent upon the ways and means position of the state government⁷.

The problem with the way decentralization has been conceptualized in India is that the prescribed local functional domain extends far beyond that definable as purely local in terms of spatial reach and there has been no attempt to define a commensurate local fiscal domain. Thus inter-governmental grant becomes necessary for vertical equity and that carries with it the possibility of reduced tax effort. The quantum of grants being received by the Panchayats is inadequate or does not commensurate the functional responsibilities cast on them.

In a significant number of cases, the state governments have not honored their commitment in terms of their own Action Taken Reports on SFC recommendations by releasing additional grants to their Panchayats. There are instances where the grants provided by the union government are not fully, properly and promptly transferred to the Panchayats. In a study of 18 Panchayats under Rayagada Panchayat Samiti, it was found that most of the finances of Panchayats consisted of government grants only. Three Panchayats had not collected a single pie from any source other than depending on state or central government assistance⁸.

Many grants accrued to Panchayats have to fulfill state level priorities rather than the grant being given to fulfill what prima-facie be a local priority with regards to borrowing powers of local governments, monetary limits up to which and the sources from which loan capital could be raised, the rates of interest payable and the methods through debt redemption should be effected are all prescribed by the state government.

⁷ Subrahmanyam, K Siva, '*Status of Fiscal Devolution on Panchayats*', in NIRD, '*Position Paper on Panchayati Raj in Different States in India*', Hyderabad, 2001, p.10

THE CONSTITUTIONAL PROVISIONS ON THE FINANCES OF LOCAL GOVERNMENT

Article 243H provides nothing new, but only reconfirms and institutionalizes the practices that were in existence even prior to the enactment of the Constitution 73rd Amendment Act, 1992. In other words, like before, the prerogative to decide taxes, duties, fees and tolls leviable under legislation made under entries in the State List of the 7th Schedule to the Constitution that should be assigned to the Panchayats and in what manner lies with the state legislature. The Constitution also permits the legislature of the states to put such 'conditions and limits', as they deem proper, before assigning specific fiscal powers⁹. The Constitution does not specifically earmark some of fiscal powers of the state list either exclusively for the local government or under state-local concurrent jurisdiction. In the state list, there are some entries on the levy of taxes/rates covering subjects that can be administered better locally. But the concept of exclusive and/or state-local concurrent tax domain for the Panchayat is absent. The purpose behind Article 243H was to ensure that the issue of financial viability of PRIs is not overlooked by the state legislatures. But by giving blanket power to the state legislatures, the said article has been made practically sterile. It is not capable of serving its purpose since the state governments do not want to share their fiscal powers with the local government institutions¹⁰.

The states legislation provide for levy and collection of certain taxes, fees and tolls but the rules relating to fixation of rate structure are not periodically done and reviewed. The EFC looked at the following local taxes and user charges for consideration of all states¹¹-

⁸ Mishra, P, '*Operational Aspect of Panchayat Finance after 73rd Amendment-a Study of Rayagada Panchayat Samiti*', in Mohanty, B, ed. '*Financing the Grass Roots Government*', APH Publishing Corporation, New Delhi, 2001, p.167

⁹ NCRWC, op.cit. para-4.11

¹⁰ Ibid. para-4.12-4.13

¹¹ Government of India, '*Report of the Eleventh Finance Commission*', 2000, para-8.16

- a) Property house tax- it is the single most important local tax today in a majority of the states. Yet it has remained beset with a variety of problems that have prevented the local bodies to exploit its full potential. In most states, the tax rates have not been revised periodically and there is no standard mechanism for determination of property tax rates and their revision. Most states have accorded a variety of tax concessions leading to revenue loss to the local bodies. Arrears of taxes are allowed to accumulate either due to inefficiency or due to delay in assessments and in appeals. Yet another impediment is the rent control laws.
- b) Some states have introduced a levy in lieu of octroi, usually the entry tax, the net proceeds of which are transferred to the Panchayats in some states. Though the grants in lieu of octroi are given to the local bodies was raised by a certain percentage from year to year, it does not have much buoyancy as the octroi had.
- c) In many states, the local bodies meet the operations and maintenance cost of drinking water supply and many other civic services. However the user charges are not revised properly and a significant percentage of demand remains in arrears.

Revenue from other sources like tax on animals, tax on advertisements, non-motorized vehicle tax and tolls is not adequate to meet the expenditure commitments of local government. Taxes are not administered properly, outdated basis of assessment, low tax rates, laxity in tax collection and nonchalance in utilizing optional tax power are some factors that are adversely affecting their resource mobilization efforts. The middle and apex layers of rural local government don't enjoy this privilege in most states. In a few states they are however empowered to levy a few surcharges on state or GP taxes.

With regard to borrowing powers of local governments, monetary limits up to which and sources from which loan capital could be raised, the rates of interest payable on such loans and the method through which

debt redemption should be effected are all prescribed by the state government¹².

According to the estimates of NIRD, the requirements of funds for the operation and maintenance of the core services (primary education, primary health, safe drinking water, street lighting, sanitation and burial ground) of Panchayats comes to Rs.1,42,128 crores or Rs.28426 crores per annum. Even a 10% of this would work out to Rs.2842 crores, more than double of what was earmarked by Eleventh Finance Commission that is Rs.1300 crores for civic services¹³.

As for the state aid which takes the form of assigned revenues and grants, local governments are always at the receiving end. State taxes from which revenue is to be transferred, the respective share of each layer of local government in the divisible pool of state taxes and tax supplements are unilaterally determined by the state government. In several states thus local governments do not have any voice in the revenue administration of the taxes levied and collected by the state government for being transferred in full or in part to them.

PARALLEL STRUCTURES

The emergences of Panchayats as a third tier of governance throws up anew several issues of inter- governmental transfer of finance in the Indian federal polity. In practice it has been found that ministries at the center and the departments in the states concerned with various rural development schemes and programs such as agriculture, health, education, women and child development and welfare etc are setting up parallel structures, at the district level.

Parallel bodies refer to those bodies whose functional domain overlaps with that of the Panchayats or which is presently functioning in

¹² Subrahmanyam, K Siva, op. cit. Pp.6-8

¹³ Oommen,MA, '*Eleventh Finance Commission Transfer System and Local Bodies: a Critique*', ISS Discussion Paper No.-6,ISS, New Delhi, 2000, p.8

such a way as to hinder\support the decision making powers\effective functioning of the Panchayats in areas which are constitutionally demarcated to Panchayats as per 11th schedule¹⁴. Funds are placed under their disposal by ministries and departments and if allocated to Panchayat Samiti or Gram Panchayat – they do so as “tied grants”¹⁵. The line ministries at the center and the line department at the states also undertake many centrally sponsored or state sponsored schemes. These schemes have staff belonging to line department in the states going right down to the block\ village level. They bypass Panchayats all the way.

The concerns highlighted in the functioning of parallel bodies were that they represented processes external to the constitutionally mandated roles of Panchayats and enabled bureaucracies to override democratically elected representatives; the trespassing of such bodies on the existing functions expected of Panchayats vis a vis administrative and financial function etc¹⁶.

The process of restructuring multi-level public finance cannot be seen independently of administrative restructuring. There are several parastatals duplicating services which the union or state governments are doing. Duplication or triplication of administrative costs must be avoided. The ultimate goal is to work towards an administrative decentralization along with functional and financial decentralization omitting vertical, horizontal and parallel structures.

It is seen that where parallel bodies have been formed, the creators tend to maintain the link of parallel bodies to PRI through members representing the sarpanch or elected members in the parallel body. It is obvious that in such cases they have little to say in the management and decision making process of the parallel body. Moreover the advantage of having women and other marginalized sections as specified in the

¹⁴ PRIA, ‘*Strengthening PRI: Awareness, Capacity Building and Devolution*’, New Delhi, 2001. p.20

¹⁵ ISS, ‘*Status of Panchayats in the States and Union Territories in India*’, Concept Publishing Co., New Delhi, 2000, p.16

Panchayati Raj Amendment is completely lost in the composition of parallel bodies. Through parallel bodies, the respective state governments are trying to bring bureaucracy and officialdom back into the local governance mechanism. On the finance side, most parallel bodies are in a better financial position than Panchayats. This is in a situation where Panchayats are to deal more with tied funds and has less of own resources¹⁷.

State electricity boards, housing boards and KVIB etc. envisage no specific role for Panchayats although electricity, housing and khadi and village industries etc. are listed as Panchayat subjects. Development activities related to tribes, scheduled caste, women continue to be implemented through special central and state agencies. Such practices undermine the role of Panchayats besides adding to administrative cost and complicating procedures.

District Rural Development Agency

DRDA is an agency independent of Zilla Parishad. Government of India and the State government jointly set up DRDAs. These are societies registered under the Society's Registration Acts of the concerned state. A project director of the rank of additional district magistrate heads DRDA¹⁸. The Union Minister for Rural Areas and Employment categorically stated in May 1998 that DRDAs were to be revamped and placed under ZP. In some state, changes, though reluctant have taken place. Any move to transfer DRDAs to ZP is met with resistance from the state legislature and other vested interest. For example in Himachal Pradesh, ministers and MLA's were against giving power over to DRDAs as this might make PRI's stronger. Only when the ZP threatened to resign, the Chief Minister offered to reschedule the decision of appointing a minister as chairperson

¹⁶ Mathew, D, '*Parallel Bodies and Panchayati Raj Institutions-an Overview*', Participation and Governance, Vol.-7, July 2000, p.3

¹⁷ ISS, op. cit. Pp-16-17

of DRDA¹⁹. In many states DRDA has become a cell under the district Panchayat however its identity as a registered society remains intact. A collector or deputy commissioner in most states except Kerala, MP and Karnataka generally heads it. Currently the entire plan budget of the Panchayat consists of plan assistance from the central and state governments by way of sponsored schemes and projects. The largest of these- IRDP and JRY are managed through DRDA even after 73rd Amendment Act. Since almost all DRDA schemes fall under the poverty alleviation programme entrusted to Panchayats, therefore continuation of DRDA as a parallel agency has no meaning. While programs like IRDP and JRY assign the role of identifying beneficiaries to the Panchayats, there are others which hardly take cognizance of PRIs-SFDA, DPAP and ITDP which lie outside the purview of these institutions. These bodies also have no authority on the rural or commercial banks, which finance poverty alleviation programs and provide priority sector loans and operate in the Panchayat areas²⁰.

Watershed Development Programme

The Ministry of Agriculture and Ministry of Rural Development mostly implement Watershed Development Programs. Even though there is no difficulty in allocating funds meant for watershed development in the district to Zilla Panchayats it is not being done. The implementing agency should receive funds from the Zilla Panchayats and thus ensuring that the responsibility of these programs remains with the democratically elected body²¹.

¹⁸ Institute of Public Auditors of India, '*Study Report on the Accounting System and Training in Panchayats in Rural Sector*', 2001, p.8

¹⁹ *Panchayati Raj Update*, ISS, January, 1999, p.4

²⁰ Rao, S, '*State-Local Fiscal Relations: Implications for the Decentralization*', in Konrad Adenauer Foundation, '*State-Local Fiscal Relations in India, December, 1996*', Manohar Publishers, New Delhi, 1998, p.30

Joint Forest Management

Joint Forest Management committee works under the Ministry of Environment and Forests. They are not accountable to the Gram Sabhas or Gram Panchayats or Samiti. Even when there is greater role for Panchayats in the area of afforestation and social forestry especially in scheduled areas, JFM operates independently of local elected bodies²².

District Primary Education Programme

The 73rd Amendment Act 1992, enjoins the state government to transfer education, which includes primary and secondary schools, technical training, vocational education and adult and non-formal education to Panchayats. NCERT carried out a study in four states- Haryana, Maharashtra, Karnataka and Bihar and found that it is functioning as a parallel body with no active linkages with Panchayati Raj Institutions²³.

Some of the structures created by state government schemes are- In Tamil Nadu, the Anna Marumalarchi Thittam (renaissance) scheme and Nammaku Name scheme (we for ourselves) have been launched²⁴. In Andhra Pradesh, the state government launched Janma Bhoomi programme on 1st January, 1997, which makes the district collector sole authority for sanctioning its schemes and monitoring their execution²⁵. The status, power and authority of PRI's are further undermined by the state government's recently created stakeholder organizations like Water User's Association, Watershed Committee and Village Education Committee. These organizations are hierarchically organized from village to district and almost functioning independently. Poor or lack of co-ordination between PRI's and these organizations sometimes not only creates a

²¹ ISS, op. cit. Pp.16-17

²² Ibid.

²³ *Panchayati Raj Update*, ISS, August, 1999

²⁴ ISS, op. cit. p.279

²⁵ Ibid. p.58

conflict situation but also considerably affects the cause for which these organizations are created²⁶.

In Karnataka, the Malnad Development Board, Maidan development and area development bodies continue to function with PRIs²⁷.

In Kerala on the other hand, the state government realizing that such parallel structures are detrimental to growth of PRIs a conscious decision has been made to abolish these institution. A large number of powers and functions along with institutions, staff and resources have been transferred at one go under the Peoples Planning Campaign, 1995, to the PRIs²⁸.

A study carried out by PRIA of the finances of parallel bodies' shows that most parallel bodies are in a better financial position than Panchayats. E.g.-Gram Vikas Samiti initiated by Haryana government, it is expected that major sources of state funds would flow to Gram Panchayats without official intervention. While it is true that Gram Panchayats is entitled to central funds and gram fund that is appreciable, one cannot overlook the fact that the funds devolved to Gram Vikas Samiti is sizeable (128crores), it adversely affects the Panchayats ability to generate income²⁹.

MPLADS

Panchayats face another challenge in receiving funds in the form of MPLADS. Member of Parliament Local Area Development Scheme was announced by the Prime Minister in both houses of Parliament on 23rd December, 1993. Each Member of Parliament had the freedom to suggest to the district collector works to be done by a sum not exceeding Rs. 1 crore per year within his or her constituency. 23 specific schemes such as

²⁶ PRIA, '*Functional and Financial Status of Andhra Pradesh PRI's*', New Delhi, 1999, p.7

²⁷ ISS, op. cit. Pp.141-142

²⁸ Ibid. p.162

²⁹ PRIA, '*Strengthening PRI: Awareness, Capacity Building and Devolution*', New Delhi, 2001, p.36

construction of school building, village roads, bridges, common shelter for the old, building for Gram Panchayats or hospital or culture/sport activities, digging tube wells etc, besides any other scheme specified by the Union government from time to time, comes under local area development scheme³⁰. Today the total amount under MPLADS for a Member of Parliament is Rs.2 crores (since December 1998). Accordingly, the Ministry of Rural Development, which operates it, is releasing the funds through the district collector. Rs.10 lakh was the maximum for any single work. All 23 items of work meant to be implemented by the MP's with the MPLAD's funds are from 29 subjects of the 11th schedule³¹. MPLADS is an assault on the letter and spirit of the 73rd Constitutional Amendment.

When the MP's have at their disposal huge funds and own priorities, it makes planning difficult and several reports suggest that MPLAD's funds are being misused or have remained unutilized by the MPs. Huge financial leeway enjoyed by MP's, while Panchayati Raj Institutions are largely starved of funds clouds the equations between the government and Panchayats and leads to erosion of the autonomy and authority of the Panchayats³². A number of state governments following the example of the centre hand out funds to the MLA's. For instance- in Orissa, Untied Construction Fund of Rs.1 lakh, while in Maharashtra, MLA's accessibility to a discretionary fund of Rs. 50 lakh³³, in West Bengal; MLA's constituency area development fund from the year 2000-01 of Rs. 15 lakhs, etc³⁴. If following their seniors, the newly elected members of the PRIs ask for their share of local development on a per capita basis, a demand which has greater credibility, the process of distortion of planning and development will be complete. This trend is a blatant violation of local

³⁰ ISS, op.cit. p.18

³¹ Venkataramaiah, ES, 'MP's Constituency Development Scheme Assaulting the Constitution', The Indian Express, February 13, 1997

³² Oommen, MA, and Mahi Pal, 'Local Area Development Scheme, Dangerous Portent', EPW, January 29, 1994, p.223

³³ Rao, S, op. cit. p.28

democracy, which has been assiduously promoted by the same set of people. As a result integrated local level planning and priorities suffer³⁵. These are not new funds, but mostly plan allocations whose priorities are now left to be determined in the most unplanned way. Concerns have been raised that these funds are being misused or have remained unutilized. The Comptroller and Auditor General of India in his first ever report on the five year old MPLADS, tabled in Parliament on 11th June 1998, pointed out clear cases of fraud in the schemes implementation involving over Rs. 50 lakhs of public funds in states like Bihar, HP, Karnataka, Manipur, Nagaland and West Bengal. Of the total amount of money Rs.2835.30 crores which was released during 1993-97, as much as Rs. 1039.10 crores remained unspent³⁶. In 332 districts of 24 states 4569 projects were executed which had not been recommended by the MP's. 302 projects were abandoned midway resulting in loss of Rs. 5.75 crores. Favourism seems to be at play in many cases where contractors were engaged instead of government agencies in violation of standard guidelines³⁷. Under MPLADS the money under other such central schemes should have gone to Panchayats as untied funds. In Maharashtra while local bodies suffer from a chronic shortage of funds, as little as 1\3rd of the funds released under MPLADS were utilized in the state. The report of the CAG tabled in winter session has pointed that the union government released Rs.214 crore for the period 1997-2000 but its utilization under MPLADS was only Rs.73 crore³⁸.

³⁴ *Panchayati Raj Update*, ISS, April 2000, p.8

³⁵ Oommen, MA, '*PRI, EFC and Working Towards a New Fiscal Federalism*', in Srivastava, DK, ed. '*Fiscal Federalism in India: Contemporary Challenges*', NIPFP, New Delhi, 2000, p.408

³⁶ *Panchayati Raj Update*, ISS, June 1998, p.7

³⁷ *Ibid*, July 1998, p.5

³⁸ *Ibid*, January 2002, p.5

RELUCTANCE TO LEVY TAXES

There have been cases where even though the legislation on Panchayats authorizes them to levy taxes, they were either unwilling or reluctant to levy taxes. This leads to deflation of possibility of resource mobilization to that extent. This way the revenue recovery of the Panchayats suffers and reflects directly on their resource position³⁹. The rural elite who generally dominate the Panchayats are more often unwilling to tax themselves or their class. The elected representatives have completely ignored this aspect for political reasons. Even the most viable indigenous resources such as the village common land have declined due to either negligence or deliberate blinking. In many places infact these lands are getting depleted due to privatization and unauthorized possession. Study carried out by Institute of Public Auditors of India in UP revealed that none of the village Panchayats sample-checked raised resources through levy of taxes on melas, haats or auction of ponds etc⁴⁰.

In a study in Andhra Pradesh by SP Ranga Rao it was found that in 20% of the villages, competent and popular leaders could convince the villagers, managed to collect taxes and honestly spend the money to the advantage of the village. In other 30% Panchayats, the Sarpanch complained that due to poverty, the local population is not able to pay taxes. Sarpanches cannot successfully enlist the cooperation of people in development work after coercing them to pay taxes. Being one of them he has his own vested interest also which prevents him from acting firmly and impartially. In many Panchayats the cost of collection maybe many times the tax collected⁴¹.

In Karnataka, Abdul Aziz found that since the elected representatives are too close to the people, they find it difficult to impose and strictly collect

³⁹ Dubey, AK, and S Mishra, '*Planning and Finance for PRI*', Kurukshetra, April, 1995, p.87

⁴⁰ Institute of Public Auditors of India, op. cit. p.21

⁴¹ Ranga Rao, SP, '*SFC : a Study in Role Perception*', in Konrad Adenauer Foundation, '*State-Local Fiscal Relations in India, December, 1996*', Manohar, New Delhi, 1998, p.31

taxes. The citizens now expect from the representatives whom they have elected to reduce the existing tax burden that enhance it. They even tend to refuse to pay taxes and rates on the ground that the quality of services provided (water, sanitation etc.) is low⁴². Panchayats thus could not fully utilize their available revenue raising powers for the following reasons⁴³-

- absence of suitable guidelines or rules framed by the state governments,
- lack of secretarial and other staff,
- unwillingness of the elected Panchayats to levy and collect non-taxes in their localities,
- unwillingness of the local people to pay Panchayats taxes due to the absence of minimum basic services and due to their poverty.

STATUS OF STATES

In a situation where political leadership is in the race for more powers and supremacy, state-local relations on the line of center-state relations are bound to generate more tensions. Inadequacy of finances has been a major impediment in the effective functioning of local bodies. The task of SFC's has been made complex due to the fact that the states themselves continue to be financially starved⁴⁴. The financial position of many backward states is quite precarious. They are incurring huge fiscal deficits and are depending for a significant extent on the central government for finances. The state government's ability to transfer funds depends first and foremost on their own fiscal health. In devising policies, state governments have been guilty of not only overlooking their own fiscal interests but also jeopardizing in the process their capacity to devolve funds to the local bodies. The state governments subsidize

⁴² Aziz, A, 'Income Structure of Rural Local Government', in Konrad Adenauer Foundation, 'State-Local Fiscal Relations in India, December, 1996', Manohar, New Delhi, 1998, Ibid. p.19

⁴³ NIRD, 'All India Panchayat Adhyakshas Sammelan : Theme Papers', Hyderabad, 2002, Pp-20-21

irrigation, electricity and food grains etc. the political nuances of such pricing and fiscal burden need to be viewed with regards to the functions of the Panchayats whose mandatory functions under the 11th schedule include drinking water, rural electricity, health and public distribution system etc⁴⁵. An inadvertent out-come of such shortsighted policy making has been to create avoidable problems to Panchayats in delivering the services that they are mandated to. In fact development finance and the emerging 'political populism' don't enable the state government to transfer some of the lucrative tax sources to local government⁴⁶. Almost all 12, 618 village Panchayats and 385 Panchayats unions in Tamil Nadu are choking without funds as the government is yet to release annual grants of over Rs. 400 crores. And, the fund starved government which itself is scrounging resources to pay salaries to its jumbo staff, has devolved only about 25% of the Rs. 517.32 crores SFC grant it allocated in the budget⁴⁷. To compound this deplorable situation, the few levels of income coupled with poverty and the consequent low taxable capacity among significant sections of society, also contributed to the resource crunch of local bodies.

STATE CONFORMITY LEGISLATION

States have passed conformity legislation in keeping with the 73rd Constitution Amendment. Some times these acts have made laudable provisions. However clauses and sections have been introduced which effectively abridge or even nullify the powers given in some states. For instance the Haryana Panchayati Raj Act 1994, made provisions for gram funds, samiti funds and Zilla Parishad funds but the size of the funds depends on the mercy of bureaucracy and the state government. The PRI

⁴⁴ Richter, J, 'State-Local Fiscal Relations in Contemporary India', in Konrad Adenauer Foundation, December 1996, op. cit. p.9

⁴⁵ Rao, S, op. cit. p.29

⁴⁶ Subrahmanyam, K Siva, op. cit. Pp.5-6

do not have clear powers of imposition of taxes. The CEO may refuse to sanction or return to Panchayat samiti any proposal about finances and taxation and his/her prior sanction is required in case of certain levies imposed by Panchayats, which are "subject to the general direction and control of the government"⁴⁸.

Thus by invoking the constitutional provisions, the state government has set limits and procedures that erode the fiscal powers of the PRI's so much so that the real and effective power to impose taxes and levies ultimately rests with the State government. What becomes apparent is the fear that the bureaucracy and the political leaders at the top level have of the local government and thus the resistance to grant them financial and functional autonomy.

FORMATION AND WORKING OF SFC

State governments are yet to compromise to the fact that the local institutions have finally come via the Constitution to share their functions as well as the finances. Most of the states reliable data on finances of local bodies is not available. The Punjab SFC's has reported that it had to carry out its task under severe data constraints. The Commission's efforts to collect data for its own deliberations were costly and time consuming. It is a matter of serious concern that the states are not giving adequate attention to the SFC's pivotal role in strengthening the local bodies. For instance if one wants to know the present status of SFC's there is no way one can get it⁴⁹. The SFC constituted in most of the states during 1994-95 has submitted their reports though they had to perform under great constraints. The virtual absence of a neatly delineated list of specific functional responsibilities has made the task of the SFC rather difficult. In many State Acts, the 11th schedule of the Constitution has just been

⁴⁷ Venkatesan, R, '*Tamil Nadu Financial Crises Chokes Panchayats Too*', The Hindu, February 2002

⁴⁸ Rao, S, *op.cit.* p.28

⁴⁹ *Panchayati Raj Update*, ISS, August 2000, p.6

copied out or at best incorporated in their respective Panchayat Acts⁵⁰. In either case barring a few exceptions, specific functions have not been devolved to Panchayats in the majority of states. This would mean that some state governments have continued to remain as indifferent to the financial needs of the newly created PRI's as they used to be. The EFC observed that ⁵¹-

- * No time limit is prescribed either in the Constitution or in the states legislation for submission of the explanatory memorandum on the action taken by the state governments on the recommendations of the SFC
- * In some states action taken report on SFC recommendation are yet to be submitted to the state legislature despite the fact the reports have been available for about 2 to 3 years.
- * Even where some recommendations have been accepted the implementation had been tardy.
- * Several important recommendations of the SFC relating to sharing/transfer of resources are often reported to be under consideration for months or even years.

In several cases the pace of such implementation is very slow although the second generation SFC's have already come into existence in many states. The state government of Sikkim has accepted recommendations of SFC but necessary orders are yet to be issued, whereas the state government of Goa is yet to accept such recommendations. In the case of Union Territories of Andaman & Nicobar Islands, Daman & Diu, Dadra & Nagar Haveli and Lakshwadweep the recommendations of the finance commission have been accepted by the Ministry of Home Affairs⁵².

Many SFC reports have not addressed the specific terms listed in Article 243- I nor have they provided a clear idea of the powers, authority and responsibility actually entrusted to the local bodies. Many of these reports

⁵⁰ RGF, '*Road Blocs to the Institutions of Self-Government*', New Delhi, 1999 p.1

⁵¹ GoI, '*Report of the Eleventh Finance Commission*', 2000, par.-8.11

⁵² GoI, '*Report on the Task Force on Devolution of Powers and Functions upon PRI*', 2001, p.9

do not clearly indicate the principles formulated for sharing or assignment of state taxes, duties, tolls, fees and the grants-in-aid. Almost all SFC's have suggested privatization of some of the Panchayat services like soil-waste disposal, cleaning of drainage and maintenance of roads. It is given in the appendices of almost all the reports without going into details of what it means and how to go about it. In Andhra Pradesh the Local Bodies Coordination Committee complained that state government has not taken any action on the SFC report submitted in May 1995⁵³. The CM, it was charged was demanding more powers from the center but was not agreeable to similar demands made by local bodies. The Himachal Rajya Panchayat Parishad have complained against the state government that⁵⁴-

- a) the government allocated only Rs.6.21 crores as against Rs.26.26 crore recommended by EFC for 2000-02
- b) Panchayats are not being allowed to function independently as several nominated committees have been set up to oversee the implementation of a number of schemes that come under functional domain of Panchayats.
- c) The second SFC has been constituted even while the implementation of the recommendation of the first SFC is long overdue.

These demands have been made by Panchayats in almost all the states. Ironically, even the SFC's have not taken the question of fiscal relations between state government and local bodies and have voluntarily set aside the question of finances of rural self-governing bodies. For example, the Gujarat SFC, although the terms of reference included examining the financial relationship between the state government and local bodies and suggest measures for improving the finances of these bodies, the commission decided not to go into the question of financial relationship between the two units. Also noticeable is the failure to go into the financial status of the rural local bodies or suggest measures to

⁵³ *Panchayati Raj Update*, ISS, February 1999, p.1

⁵⁴ *Panchayati Raj Update*, ISS, January, 2002, p.3

improve their financial health. The SFC decided to confine itself to examining issues relevant to putting finances of urban local bodies on a sound footing in view of the high degree of urbanization in Gujarat- although two third of the states population lives in rural areas⁵⁵.

In case of the formation of SFC's, Article 243-I (2) makes requirements for the State legislature to prescribe the qualification for a person to be appointed as the chairman or a member. While some states made such provisions in the State Panchayats Acts, but many states have left it to the state government to prescribe these details by rules. This has led to wide diversity in this matter. For instance, in some states, serving government officers are appointed as chairperson and members of the SFC and that too in ex-officio capacities. This puts limitations on the ability of the SFC to act as an autonomous body to make recommendations in a free and independent manner as has been envisioned in the Constitution⁵⁶.

The EFC is required to make its own assessment about the manner and extent of augmentation of the consolidated funds of the states, keeping in view the provisions required to make for the emoluments and terminal benefits of the local bodies including teachers, the existing powers of the local bodies to raise financial resources and the powers, authority and responsibilities transferred to local bodies. EFC found that the State memoranda do not generally indicate the requirement of funds for the emoluments and terminal benefits for the employees including those of teachers. It does not give the position in regard to transfer of powers, authority and responsibility or the financial powers devolved on the local bodies to raise resources. In quite a few states action is yet to be taken⁵⁷.

POLITICAL LEADERSHIP

Ministers and MLA's are worried that the power they enjoy so far

⁵⁵ Rao, S, op. cit. p.27

⁵⁶ GoI, '*Report of the Eleventh Finance Commission*', 2000, para-8.12

will diminish if the Panchayats become powerful. The state level leaders don't like the leadership to emerge from the lower levels, which would pose challenges to them in the due course. They don't want active and functioning local bodies to be nurseries of leadership. In Orissa for example, when the new government came to power in 1995, it decided to dissolve the duly elected Panchayats. The real reason for this action was that the MLA's were impatient to wrest full control of large sums of money coming to the Panchayats through the central government schemes for rural development⁵⁸. Local leaders have often accused the government of delaying and dithering over matters relating to the devolution of financial, executive and administrative powers to PRIs.

In Punjab, it was found that the Minister for Rural Development and Panchayats manipulated the Rs.76 crore meant for the centrally sponsored JRY schemes, which was to be made directly available to ZP and arbitrarily redistributed it⁵⁹. In Punjab even cases had to be filed by the local representatives seeking the direction of the courts, for the delegation of executive, financial and administrative powers⁶⁰. In Andhra Pradesh, diversion of funds it was alleged by the Andhra Pradesh Panchayat Sarpanches Association was weakening local bodies in the state besides taking control of funds of GP⁶¹.

CONCLUDING OBSERVATIONS

The above discussion highlights that Panchayats are far from autonomous in performing their functions primarily due to the inadequate

⁵⁷ Ibid.

⁵⁸ Mathew, G, 'Restructuring the Polity: the Panchayati Raj in Rajasthan', in Sebasti, I Raj SJ and E. Mathias, ed. 'People's Power and Panchayati Raj-Theory and Practice', ISS, New Delhi, 1998, p.46

⁵⁹ Verma, PS, 'Panchayati Raj in Punjab', in Sebasti, E Raj SJ and E Mathias, ed. op.cit. p.155

⁶⁰ Ibid. p.162

⁶¹ Panchayati Raj Update, ISS, August 1998, p.1

availability of funds. To sum up the problems faced by Panchayats, it may be said that⁶²-

- a) The extent of fiscal decentralization through the empowerment of the PRIs has been very little.
- b) The fiscal autonomy of PRIs is far from adequate because they cannot balance their revenue budgets by using their own fiscal powers.
- c) The PRIs are principally grant fed and their dependence upon the state government even for carrying out their routine function is quite heavy.
- d) Among the three tiers of Panchayats, the GP are comparatively in a better position, because GPs have some taxing power of their own, while the other two tiers are dependent on tolls, fees and non-tax revenue for generating internal sources.

Some of the other common handicaps are⁶³ –

- e) Own sources are limited in quantum with the result of poor taxation and poor realization of whatever tax has been imposed.
- f) The state government in effect controls the programme funds. They normally follow the state dictates about the break up.
- g) Substantial amounts of taxes like sales tax, motor vehicle tax, excise revenue etc. are not shared with Panchayats.
- h) Devolution of funds upon Panchayats is meager in quantum and inflexible in nature, which hardly leaves any room for the Panchayats to expand the amount as per their priorities.

Local government in general and Panchayats in particular continue to be the seat of financial problems since the days of their full fledged establishment in immediate post independence era in India. In spite of the Constitutional provisions (1992) they continue to depend too much on devolution of funds from the states, they cannot be construed to be effectively enjoying financial autonomy even if the amounts received from

⁶² NCRWC, op. cit. para-4.8

⁶³ Dubey, AK and S Mitra, op. cit. p.88

the state are adequate. The dependency syndrome under such circumstances, which afflicts the PRIs, they will degenerate into 'agents of the state government'⁶⁴. An analysis of the finances of Panchayats reveals that in raising their own resources the performance of Panchayats was not encouraging in relation to the tasks assigned to them. They subsist especially when seen mostly on the meager grants and assigned revenue given by the state government. The financial autonomy of the Panchayats hangs on a single thread of their own resources from taxes, duties, tolls and fees authorized by the state legislature to be levied, collected and appropriated by them. Thus the scope of the PRI to function as units of self-government is extremely circumscribed⁶⁵.

One of the emergent tasks of the center, state and local governments would be to adopt measures to augment the financial resources of the Panchayats. Not much thought was probably given to the kinds of issues of fundamental nature that they might throw up afresh. NCRWC has raised the following questions regarding the constitutional status of Panchayats. Were we, by constitutionalising the Panchayats and by defining them as 'institutions of self-government' opting for multi-level federation in place of the existing two-level federation? Did this imply conferring co-ordinate status to the local government institutions? If so, what were its implications in respect of division of powers and functions among different levels of government? If the Constitution did not think about conferring co-ordinate status to the local government institutions contrary to the expectations of many advocates of decentralization, what kind of status it sought to give to these institutions?

Certainly the Constitutions did never intend that the Panchayats would be like any other authority created by a statute of the state with only difference as regards the Constitutional government's unfettered power to restrict or limit its autonomy. If the position of the Panchayats

⁶⁴ Aziz, A, op. cit. p.18

⁶⁵ Barnabas, AP and OP Bohra, '*Finances of Panchayati Raj Institutions*', NIPFP, New Delhi, 1995, p.57

was above that of usual statutory authorities, then how much above the floor, short of the level of coordinate status, should the local government institutions rise? The Constitution left these questions unanswered⁶⁶. But they are questions nevertheless that need to be addressed if Panchayats are to act as institutions of local government and democracy is to strengthen and expand in India.

⁶⁶ NCRWC, op. cit. para-1.6

CHAPTER 4

AUGMENTATION OF PANCHAYAT FINANCES

The mandatory provisions of 73rd Amendment Act have provided the necessary safeguards so that Panchayats do not have an uncertain future, yet the task of making them vibrant bodies still remains to be done. Democracy to be vibrant and deliver the outputs to its citizens must be participative, inclusive and lay emphasis on decentralization. Though the process of devolutionary decentralization has gained momentum and powers and authority are being delegated to PRI's the process lacks spirit of the 73rd Amendment. The Panchayats have fluctuating fortunes – as has been seen earlier all of them have one thing in common – their poor fiscal base¹. The PRI's which are supposed to be a vital link in the chain of national development, are being viewed by higher level government in terms of local service delivery only. As a result these institutions are too dependant on the higher governments for their financial and human resources. The need of the hour is to grant actual financial authority entailing devolution of financial power and authorities to Panchayats to act on their own. Consequently, finances of the local bodies with aspects having a crucial bearing on their effective functioning have become an important issue. Various conferences, commissions and task forces set up by the government besides research institutes, non-governmental organizations etc. have made a number of recommendations to overcome the financial crunch faced by Panchayats. Suggestions range from amendments in the Constitution to strengthening the local resource base of the Panchayats and making them financially self-sufficient. Even if a very good conformity act is formulated and implemented, there are still resource needs to be met.

¹ Rai, M, M Nambiar, S Paul, SS Singh, S Sahni, '*The State of Panchayats a Participatory Perspective*', PRIA/Sanskriti, New Delhi, 2001, p.182

For one, functional transfers may not be matched perfectly by financial transfer. Second, own resources of Panchayats many of them proverbially starving for resources may find their resources inadequate to meet the growing demand for basic services, local area planning, poverty alleviation programme, administrative strengthening etc². The fiscal capacity of the PRI's firstly, even at their present level of functional responsibilities is poor and they are disproportionately dependent upon the State government and secondly, their fiscal autonomy is negligible.

Major fiscal restructuring and financial resources are necessary to enable the Panchayats to function as viable local self-governments. Some of the measures necessary for such reforms maybe taken within the existing Constitutional provisions. But, there are areas where rethinking about the Constitutional framework itself would be necessary.

GREATER AUTONOMY IN DECISION MAKING

An important aspect of transfers is that they should not endanger the autonomy of the PRIs. A devolution mechanism that promotes a dependency syndrome or grantmanship is the very anti-thesis of autonomy. Autonomy does not mean license but presupposes accountability and responsibility. They should be so designed so as to promote incentives for efficient fiscal management and discourage waste and inefficiency³.

² Bird, RM, '*Financing Local Services Patterns, Problems and Possibilities*', in Amanand, ed. '*Financing of Panchayati Raj*', Excel Books, New Delhi, 2000, p.65

³ Oommen, MA, '*Devolution of Resources from the State to the PRI's*', ISS, New Delhi, 1995, pp.12-13

⁴ Subrahmanyam, KS, '*Status of Financial Devolution on Panchayats*', in NIRD, '*Position Paper on Panchayati Raj in Different States in India*', Hyderabad, 2001, p.103

Taxes, duties, tolls and fees assigned to Panchayats⁴-

- (a) As the government both at the center and state levels, are making substantial investments on physical and social sectors in the rural areas, there is an imperative to make levy of certain important imposts like the tax on building and land and user charges for the provision of basic services mandatory for the Panchayats. In the absence of such mandatory provisions there will be greater reluctance on the part of Panchayats to raise revenue from their localities. Whatever the tax and non-tax items assigned to the Panchayats, they must be locally feasible, administratively simpler, fiscally productive and economical to collect.
- (b) State governments on their part can evolve an appropriate mechanism to reward the 'performing Panchayats' and to penalize the 'indolent Panchayats' through a well conceived system of incentives and disincentives. An incentive mechanism should have parameters like: levy of optional taxes, levy of taxes at a statutory-permitted maximum rates and collection of revenue dues in full. In this connection, Tamil Nadu model of matching grants on a graded basis for house tax collection by the Panchayats deserves to be emulated by others.
- (c) States may also devise appropriate mechanism for realistic reassessment of real estate taxes of the Panchayats periodically. They may also avoid prescribing fixed rates for the local taxes to leave freedom in rate fixation to the Panchayats concerned. Unwarranted and time consuming procedures prescribed for the levy of certain taxes and non-taxes may also require a fresh review to providing more freedom and flexibility to the Panchayats.
- (d) In order to ensure financial responsibility, the Panchayats which levy taxes should also be made responsible to collect them.
- (e) The important issue relating to provisions of a minimum core staffs for the Panchayats commensurate the revenue and other responsibilities entrusted to them, demand special attention of the State.
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(f) There is an urgent need to frame rules for the Panchayats as regards the modus operandi and collecting the revenue assigned to them by their respective State legislatures.

The Report of the Task Force on Devolution of Powers and Functions (2001) upon PRI has suggested that the State government should follow the following principles⁵:

- (i) Assign revenue powers to the Panchayats and identify those revenues, which have a localized revenue base. But the revenues identified should not lead the Panchayats to multiple or overlapping revenue jurisdiction among the three tiers of Panchayats. For e.g. tax on property, octroi, toll tax, advertisement tax etc. have localized revenue base and hence are ideally suitable for being assigned to the Panchayats. The taxes assigned must be locally feasible and cost effective in their collection.
- (ii) The state government should be required to prescribe the relevant guidelines/rules/powers of the Panchayats in respect of all the revenue powers that are statutorily assigned to them by their respective state legislatures. A time limit for prescribing such relevant rules/guidelines/powers of the Panchayat in respect of each revenue power granted to the Panchayats is urgently called for.
- (iii) When the Panchayats are endowed with certain revenue raising powers, efforts must be made, and incentives created, to facilitate their fuller use by the Panchayats. If a minimum quantum matching contribution is insisted from the Panchayats for availing some of the state and central branch, there may perhaps be some revenue generation effort at the local level. Such a minimum matching contribution from the Panchayats may

⁵ Government of India (GoI), '*Report of the Task Force on Devolution of Powers and Functions upon PRI*', New Delhi, 2001, p.28

be insisted on with due regard to the level of development of their respective territorial jurisdiction.

Another suggestion for strengthening the finances of PRI's is: typically X is collected by the central authorities, redistributed to the Panchayats through the state governments. Hypothetically, the Panchayats can find someone who pays X as tax, contact him/her, take the money and give him/her a certificate of payment. Such a process completely bypasses hierarchical redistributive mechanism. With Panchayats in power, supervision, monitoring and accountability rest directly with the local government. If they cannot raise funds through local taxes they should have the right to the direct use of taxes collected. This immediately reduces the associated transaction cost and is a real net gain to the treasury⁶.

Taxes, Duties, Tolls and Fees Levied and Collected by State Government for Panchayats:

While the mechanism of specific revenue sharing has its own merits, states may have to ensure that, in respect of state revenues to be shared by Panchayats, their fiscal productivity is not eroded through slackness in collection or unilateral decisions affecting their base or tax rates. Each state may identify some of its own revenues having localized revenue base and ensure transfer of the proceeds of such revenue to the Panchayats. Such taxes include land revenue, cesses thereon, profession tax, mineral tax, entry tax, stamp and registration fees and entertainment tax covering cinematography and other exhibitions.

As in the case of revenue sharing between the union and the states, the revenue transferred under this mechanism could be earmarked to general purpose of the Panchayats. Panchayats could be assured, well

⁶ Marjit, S, 'Decentralized Financing, Governance and Public-Private Cooperation', Economic and Political Weekly, May 15, 1999, p.1199

ahead of the beginning of each year, the minimum quantum of revenue- which they are likely to receive during the succeeding year under this dispensation. This facilitates a realistic planning of their own revenues and expenditure management. But these revenues cannot form a significant of the aggregate receipts of the Panchayats. The nation wide study conducted in 2000 by NIRD revealed that assigned revenues accounted for a near 4% of the combined receipts of all the Panchayats⁷.

The Ministry of Rural Development has suggested that⁸:

- (i) In the area of revenue transfer among the three tiers of Panchayats, consideration of equity in the inter-tier and intra-tier distribution of resources with due regard to the responsibilities cast on each level unit of Panchayats and their predictability by the recipient units to enable them to make their budgets realistic.
- (ii) The entire process and scheme of revenue transfer to the Panchayats should be transparent and objective. The nature and magnitude of revenue transfer to the Panchayats should not be allowed to be a substitute for their internal revenue mobilization and that they should not adversely affect the initiative of the Panchayats in utilizing their revenue raising powers to the fullest extent.
- (iii) To facilitate harmonious inter-tier fiscal relations, it should also be ensured that any mutually agreed scheme of revenue transfer should be based on the principle of consultation between the tiers involved.
- (iv) In conformity with article 243-H the State legislature should realize their responsibility and legally prescribe the taxes, fees, tolls and duties to be assigned to the Panchayats as well as the

⁷ Subrahmanyam, KS, *op.cit.* p.104

⁸ GoI, '*Report of Task Force*', *op.cit.* p.29

State revenues to be assigned to Panchayats instead of leaving these crucial issues to be decided by the executive government. Some of the State taxes which deserve to be shared with the Panchayats comprise the profession tax, entertainment tax, land revenue etc. Profession tax which is not being levied in some of their states maybe exploited by the state government concerned, and the revenue proceeds thereof maybe transferred to the Panchayats.

Grants-in-Aids:

All the State governments pay grants-in-aid to the Panchayats for a variety of purposes. A major portion of these grants belongs to the category of specific grants tied to particular sector. Some grants emanate directly from the state government, others from the line departments and grants under some centrally sponsored rural development programs. Thus, broadly speaking, the grants, which become available to the Panchayats emanate both from the state and the union governments, although the relative share of the former in the total is still very large. Despite the appointment and recommendations of State Finance Commissions, the system of grants in most of the states is not rationalized and suffers from inadequacy and uncertainty. An important aspect of transfers is that they should not endanger the autonomy of the PRIs. A devolution mechanism that promotes a dependency syndrome or grantmanship is the very anti-thesis of autonomy. In view of this, it may be ensured that Panchayats are not simply reduced to the status of mere implementing agencies of the state government.

Efforts should be made to the extent possible by the state government to provide a certain percentage of their grants to the Gram Panchayat as 'untied grants', subject to the broad guidelines which such untied funds could be utilized. Untied grants will help the Gram

Panchayats to utilize it according to their needs and local priorities. The Gram Panchayats should get the bulk of untied funds of about 70%, while district Panchayats and intermediate Panchayats should share the remaining 30% equity.

According to NIRD, there is an imperative need to make provisions relating to grants in the relevant Panchayat acts of the State itself i.e. must have statutory status. There must be some incentive for the States which effect relatively greater fiscal devolution on their Panchayat vis a vis other States⁹.

The State and Union governments should endow the Panchayats with adequate responsibilities and necessary powers in the area of their financial administration so as to ensure greater autonomy for them in the decision making process. Important among these are¹⁰ –

(A) District Panchayat (DP)

- (i) To impose taxes, cesses, levies etc. levy user charges and develop endowments for income generation.
- (ii) To prepare and finalize annual budget estimates of the DP.
- (iii) To constitute a DP Fund and operate it for authorized purposes.
- (iv) To sanction loans, contingent expenses, etc. for authorized purposes.
- (v) To borrow money from banks, financial institutions, etc., for authorized purposes.
- (vi) To inspect utilization of funds in respect of various schemes under implementation within its jurisdiction.
- (vii) To acquire, lease and/or transfer property.

⁹ Subrahmanyam, KS, op.cit.pp.107-108
10GoI, 'Report of Task Force', op.cit.Pp.32-33

(B) Intermediate Panchayat (IP)

- (i) To impose taxes, cesses, levies etc. levy user charges and develop endowments for income generation.
- (ii) To prepare and finalize its annual budget estimates.
- (iii) To constitute an IP Fund and operate it for authorized purposes.
- (iv) To inspect utilization of funds in respect of various schemes under implementation within its jurisdiction.
- (v) To acquire, lease and/or transfer property.

(C) Gram Panchayat (GP)

- (i) To impose taxes, levy user charges and develop endowments for income generation.
- (ii) To prepare and finalize its annual budget estimates.
- (iii) To constitute a GP Fund and operate it for authorized purposes.
- (iv) To borrow money from banks, financial institutions, etc., for authorized purposes.
- (v) Full financial powers for payment of salaries to all the staff working under the Panchayats, even though the funds may come from government.

Centrally and State Sponsored Schemes

While a federal government has every right to sponsor and promote schemes of national importance and priorities, quite often these types of flow of funds turn out to be the very negation of decentralization. Anti-poverty program in the country will unquestioningly acquire greater coherence if central funds for this purpose were routed through state governments for consolidation with state-local flow and if local participation were sought in the disposition of these funds¹¹. A number of

¹¹ Rajaraman, I, OP Bohra, VS Ranganathanan, 'Augmentation of Panchayat Resources', Economic and Political Weekly, May 4, 1996, p.1072

schemes are implemented by the Center and State governments relating to the subjects mentioned in the 11th Schedule of the constitution. The Task Force on Devolution of Powers and Functions upon PRI felt that there is an urgent need to rationalize all the schemes that are being implemented at the various Panchayats levels¹². Over the years the governments have built a plethora of schemes that purport to define with greater precision when, how and by whom expenditure has to be incurred. Each scheme is provided with guidelines which require to be serviced through a district budget head without realizing that this carries with it a burdensome management and accounting codes and procedures. The Members of Task Force revealed that at the district level more than 300 to 400 schemes with meager amounts are being implemented. It has become difficult to keep track of these schemes and monitor their expenditures. All such schemes having a small allocation should be merged with some broader guidelines at the district level and converted into untied grants under one head. There are a number of departments whose schemes nearly interface with some other departments, e.g. Social Welfare, Women and Child, Rural Development, Agriculture, Education, Health etc. It is felt that the common schemes having common beneficiaries/target groups can be converged to avoid complications and duplications. The Center and State governments should make its efforts towards the convergence of these schemes at the district, intermediate and gram Panchayat level. The Task Force found that more than Rs. 40,000 crores of the total annual plan outlay under the centrally sponsored/central sector schemes and about Rs. 31,000 crores of annual plan outlay of the state plans, partly or wholly, related to 29 subjects mentioned in the 11th schedule are implemented by the state government at the state and district level. It is, therefore, suggested that the proportion of the scheme funds implemented

¹² GoI, *Report of Task Force*, op.cit. Pp.33-34

at the district level should be transferred to the PRI's proportionately according to their needs.

PARALLEL STRUCTURES

The Prime Minister Shri A B Vajpayee in a letter to Shri Chandra Babu Naidu, Chief Minister of Karnataka, on 27th April 2001 had written that, 'consequent on the amendment, Panchayats have been visualized as the third tier of the governance in the federal polity. It is my firm belief that development both economic and social is best served when decentralization and devolution touch and thus change the lives of people living in the smallest villages. The implementation of financial decentralization by the States, however, reflects only a minimum devolution of powers. Since the Constitution envisages Panchayats as institutions of self-government (with unambiguous political, administrative and financial powers) it seems imperative that the devolution of powers is not delayed. I have also to point out that parallel structures, which marginalize PRI, should not be set up'¹³.

These views reflect the sad truth that while civil society organization, various ministries / department of central and state governments have adequate resources and expertise at their disposal, Panchayats on the other hand are starved of funds and technical expertise. If the programs of the above mentioned organizations and departments are formulated and implemented in collaboration with Panchayats, there will be pooling of resources, expertise etc. leading to greater quality and efficient services and sustainability of the project. Rather than creating new structures to address the problem in the present system, what is needed is a careful examination of the gaps in the existing system and formulation of practical solutions whereby the gaps can be

¹³ *Panchayati Raj Update*, ISS, June, 2001, p.3
¹⁴ Rai, M. et.al. op.cit. p.42

addressed within the framework of PRI's and outside the influence of bureaucracies¹⁴. There is no need to constitute parallel bodies in Panchayats. The existing PRI system permits the State government to constitute standing committees of Panchayats to look after different subjects. Instead of strengthening the existing system and guarding against loopholes, these parallel bodies have started undermining the constitutionally mandated Panchayat¹⁵. The Gram Panchayat fund could be strengthened by pooling all such investments under the supervision of the Panchayats so that there is direct link between project delivery and its outcomes. For example, forestlands in many places are lying unutilized. If Panchayats were provided partnership in productive management of these lands, a significant amount of own income can be generated by Gram Panchayats.

STATE FINANCE COMMISSIONS

The State governments should take expeditious measures to ensure that all recommendations of their SFC's which are agreed to, are implemented through relevant administrative, legislative and financial measures within a given time limit to be presented to the state legislatures. According to NIRD¹⁶-

- (i) The constitution of the next SFC should be at the expiration of every fifth year or earlier from the date of the first notification constituting its immediate predecessor commission.
- (ii) No State government should allow more than eighteen months for its SFC for submission of its reports.
- (iii) State statutes may reacquire the state government to lay their SFC report along with explanatory memorandum containing the action taken on

¹⁵GoI, 'Agenda for State Ministers Conference on Panchayati Raj', Ministry of Rural Development, 2001, p.30

SFC recommendations before their respective State legislature within a maximum period of six months from the date of receipt of their SFC report.

(iv) The composition of SFC should consist of academics of eminence with background and experience in public finances particularly in local government finances.

(v) State must utilize the allocation made by the EFC to build the necessary database and ensure regular flow of data on various facets of their local government finances to their SFC's and the national finance commission.

(vi) SFC's that have not submitted their reports should do so at the earliest. And where already submitted, the concerned State governments should make the recommendations public for debate in general and in the assembly in particular before accepting them.

There should also be a permanent secretariat for the SFC to gather the necessary data on local government finances so that the continuity is maintained in preparing the future SFC reports with the help of the database.

Transfer of resources on the basis of the recommendations of the SFC's provides only one of the alternatives. In view of the delicate financial situation of the State government, this measure is not going to help in a long term perspective, in particular, if the attitude of the State government is passive. Therefore local governments have to plan for mobilization of internal resources.

DRDA

In every state, huge funds are made available to DRDA. According to one estimate, the average annual expenditure of DRDA in Rajasthan for instance is about Rs. 600-700 crores. They even by-pass the budgetary controls by State government. The maintenance of accounts by DRDAs

¹⁶ Subrahmanyam, K Siva, *op. cit.* Pp. 110-111

has found to be far from satisfactory as repeatedly commented upon by the CAG of India. There is a need to make the chairperson of Zilla Parishad the chairperson of DRDAs¹⁷. If this money goes to PRI's directly, their financial situation will improve considerably. However, a number of States have taken positive steps by bringing DRDAs under complete control of Zilla Parishad. It is hoped that with the financial and other resources of the DRDAs being at the disposal of PRI's, institutions of self-governance will be able to strengthen themselves.

LOCAL RESOURCE MOBILIZATION

As the Panchayats may find it difficult to raise sufficient revenue from their taxes, they must make serious efforts to increase their own resources through other revenue powers granted to them. These powers relate to levy of fees, fines, rents from their properties and tolls. For becoming financially self sufficient, Panchayats have to raise their own resources. The 11th schedule to the Indian Constitution contains several items that have the potential of generating significant non-tax revenues for local government. Efforts should be made to create community assets such as community halls, market complexes and shops from which additional non-tax revenue could be mobilized. Attempts should be made to work out the modalities for the identification of users of the various local-government services and the class of people who could be potential contributors to local non-tax revenue. It has been found that some Panchayats were not utilizing their fund raising power for fear of becoming unpopular¹⁸. There is a need to stop this trend and help Panchayats to evolve a mechanism for local resource mobilization. To expedite the

¹⁷ Institute of Public Auditors of India, *Study Report on the Accounting System and Training in Panchayats in Rural Sector*, New Delhi, 2000, p.8

¹⁸ RGF, *Voices from Below*, New Delhi, 1999, pp.6-7

process of development in the villages, the Gram Panchayat must seriously look into matters of privatization and unauthorized grabbing of common land and augment their finances from indigenous resources. The local elite should desist from choosing a political strategy of avoiding risk by not extracting indigenous resources for development¹⁹. Panchayats can effectively use the lands available to them for remunerative purposes²⁰-

- Leasing out fishery rights of panchayat tanks.
- Leasing out the grass grown on tank bunds and other areas in the panchayat.
- Leasing out the grazing grounds for grazing cattle.
- Fees for encroachments on Panchayat lands and other public places.
- Fees for conversion of agricultural land into non-agricultural land.
- Fees on markets, registration of cattle sold in markets and the bazaars, from shop-keepers in fairs.
- Fees for registration of vehicles and boats.
- Tolls on vehicles, ferries and animals.
- Fees for temporary occupation or use of porambokes, village sites, roads and other public places.
- Fees on carts, auto, and tonga stand.
- License fees on D and O trades.
- Registration fees for births, deaths and marriages.

Intermediate and district Panchayats can construct industrial estates, market sheds, slaughter houses, shopping complexes, community halls; etc. for which they can borrow funds from their state government or banks. These remunerative enterprises can be leased out by the Panchayats to earn additional revenue.

¹⁹ Verma, PS, 'Panchayati Raj in Punjab', in Sebesti, L Raj SJ and Edward Matthias, ed. 'Peoples Power and Panchayati Raj: Theory and Practice', ISS, New Delhi, 1999, p.168
²⁰ NIRD, 'All India Panchayat Adhyakshas Sammelan', Hyderabad, 2002, Pp.22-23

There are different ways like charging fees, imposing price of services, charging rents, sale of community products, maintaining user-group deposits, borrowing capital from the community etc. for mobilizing funds. People are generally ready to contribute wholeheartedly for the development of their own village. These contributions can be in the form of labor, land or money. In Dudhiya Gram Panchayat of Indore district, the PHC was constructed on a land donated by one of the Gram Sabhas members²¹. Kodaria gram Panchayat also in Indore was able to generate Rs. 65000.00 for the Narmada pipeline and Rs. 45000.00 for the building of a high school through public contribution²². The critical factor governing such decisions is the perceived benefit to the community and its linkage to felt needs of the community. Internal financing has some good effects on the community²³ –

- 1) it not only generates a feeling of ownership but also inculcates a sense of responsibility for such community goods and services.
- 2) Such community involvement in raising internal resources creates scope for greater participation and brings local people together for achieving common interests.
- 3) It provides local people with incentives to make economic use of local resources in order to cut down costs.
- 4) It promotes indigenous technical knowledge of local communities, which in turn reduces cost of development.
- 5) Community financing based on ability to pay off community members results in better adjustment in the sharing of output.

²¹ Verma, PS, op.cit, p.173

²² Ibid.

²³ Jena, SC, 'Management of Panchayat Funds: an Analysis', in Mohanty, B, ed. 'Financing the Grassroots Government', APH Publication Co., New Delhi, 2001, p.73

- 6) Borrowing from local people is better than other sources as here there is no payment of interest towards the borrowing amount/loan.
- 7) Openness in discussion about the financial aspect of Gram Panchayats helps in devising modes of borrowing, terms and conditions of the repayments along with the modes of expenditure.
- 8) For generating and effectively utilizing financial resources, local people's priorities and views should be reflected in planning for such resources and its monitoring.

It is therefore necessary that local level resource mobilization should be done to improve the financial strength of the Panchayat. The village ecology should be protected, besides non-tax sources of Panchayat incomes like shops, fishing ponds, raising nursery and forestry on wasteland and village orchards are to be explored²⁴.

In the long run, Panchayats can improve their own resources only through non-tax resources and may not depend only on State or Central government grants.

TRAINING AND INFORMATION

Panchayats members need to be provided training in finance and accounts management. This training in finance should be participatory in nature and practice. Financial assistance to PRI's is not always clearly defined by State governments. Unlike PRI's in Kerala, Panchayats in other States do not know how much money they will get or when they will get it from the State in a particular financial year²⁵. Timely availability of financial information to Gram Panchayat/Gram Sabhas members is equally important. People need information for them to know how to use it effectively. Information resource centers should be established at block

²⁴ Mohanty, GR, '*Panorama of Panchayat Finance: a Study of Chandradupur Gram Panchayat in Orissa*', in Mohanty, B, op.cit.p.152

²⁵ Rai, M, et al op cit Pp 182-183

levels. District Planning Committees should be activated to ensure the optimum utilization of resources. They can with the help of district and block administration ensure a constructive flow of information between PRI's and government. They should be strict and smooth system of account of information. Every PRI must know in advance the total money available to that Panchayat in a particular financial year.

TAPPING LOCAL HUMAN RESOURCES

Exploitation of local resources must include not only tapping the financial and physical potential but an important ingredient of such an exercise would be to utilize locally available human resources in the form of "Shramdan". For example in Ralegan Shindi (Maharashtra) an interesting instance is provided where the entire village was transformed through effective mobilization of local labour²⁶. Although the funds have largely come from the government, construction of public wells, canals, afforestation, horticulture, building of schools and temples, has all been undertaken through shramdan. People's involvement and the sense of belonging and being active participants in the process of development have greatly contributed to the success of the unique effort led by Anna Hazare²⁷. Whether it is a question of identifying local needs and resources deciding on the kind of assets to be created, safeguarding ecological balance or being vigilant to the working of the local leadership and social audit through periodic discussions of expenditure and budget reports at the Gram Sabhas, putting people at the center of the developmental process is important.

²⁶ Rao, S, '*State local fiscal relations: Implications for Decentralization*', in Konrad Adenauer Foundation, op.cit. p.36

²⁷RGF, '*Voices from Below*', New Delhi, 1997, p.6

PANCHAYAT FINANCE CORPORATION

There is need to establish an institution like Panchayat Finance Corporation for granting loans to the Panchayats for taking up some gainful activities at the respective levels²⁸.

Productive economic activities should be initiated at village level through active negotiations and financial institutions (NABARD, Rural Banks etc.). This would be the base for generating more revenues at the Gram Panchayat level. Marketing Board Funds, Rural Development funds, wherever available should be spent with the approval of Panchayats²⁹. Development funds coming from international organizations \ United Nations Agencies should be operated in due consultation with the concerned subject \ standing committee of the Panchayats³⁰.

TRANSFER OF FUNDS UNDER MP/MLALADS TO PANCHAYATS

Either both of these funds should be dispensed with or, if not, these funds should be spent in consultation with Panchayats. Or separate development funds on the lines of those for MP's / MLA's should be made available to elected Panchayat leaders so that they could spend it in the fulfillment of the felt needs in their respective constituencies. The existence of MP\MLA LADS only leads to increased political interference and bureaucratization³¹.

CONSTITUTIONAL CHANGES- NCRWC

²⁸ Ibid.

²⁹ Raj, M, et al. op. cit p.268

³⁰ RGE, 'Dialogue on Panchayats', New Delhi, 1999, p.15

³¹ Ibid. p.16

The NCRWC appointed by the Government of India to look into the working of the Constitution has made a number of recommendations with regards to Panchayati Raj institutions in the country. It felt that experience of the last few years suggest that the provisions of the 73rd Constitution Amendment themselves require a fresh look. From the hindsight, it becomes clear that the amendment did say certain things clearly and unambiguously but preferred to express many other vital things only by the way of implications, suggestions and hints as it were. This led to various interpretations of the same provision- refreshingly liberal in nature at one extreme and highly conservative at the other end of the pole. Most States have stuck to the conservative view and refused to give concrete shape to the 'spirit' of the Constitution. It is not without some justification that the Panchayats that came in the wake of the post-73rd Constitution Amendment have been described as democratic institutions power- a decorative box, as it were, that contains nothing inside³².

The NCRWC thus made a review of the working of the Constitution provisions on Panchayats in different States and suggested specific Constitutional reform in certain matters. By leaving unattended the basic question of the status of Panchayats, the Constitution, by and large, failed to give a definite direction to the decentralization process. This needs to be corrected by drawing insights from the experience of the past eight years. Assuming that the local government institutions will have autonomy however limited it maybe; Part IX will have implications for provisions in other parts of the Constitution, particularly in matters connected with the distribution of executive and financial powers³³. Institutionalization of Panchayati Raj system will depend to a large extent on the State government. Hence reforms are necessary in their Panchayat Acts and

³² NCRWC, *'A Consultation Paper on Review of the Working of the Constitutional Provisions for Decentralization (Panchayats)*, ncrwc@nic.in.com, para-1.5

³³ *Ibid* para-1 7

rules as also in their executive orders which supplement the legal instruments.

Independent as well as concurrent tax domain for restructuring the existing 7th schedule can bring about the local bodies. The restructuring would necessitate introduction of a local list and a state-local concurrent list, which will be most helpful to provide fiscal autonomy to the local government institution. The Commission has also recognized some difficulties in carving out a list of fiscal powers for the local bodies in the 7th schedule. Between the Gram Panchayat and Zilla Panchayat there are various types of local bodies, which differ from one another in respect of size, functional responsibility and administrative or financial resources. How to distribute taxing power among them maybe difficult to determine centrally by the Constitution. Thus some kind of uniformity across the state is necessary in respect of principles for determining the base for the tax and fixing of tax rates. While some disparity among the different local bodies are natural and may, in fact, be welcome, wide disparities may hurt the principles of equity. However some power of fixing the 'procedure' or 'condition' or 'limits' maybe retained by the state legislature while earmarking certain taxes for the local bodies³⁴.

The other alternative is to make changes in the area of state discretion and guarantee devolution of fiscal powers from state to the Panchayats.

Sub clauses (bb) and (c) of clause (3) of Article 280 require the federal finance commission to make its recommendations in respect to the Panchayats 'on the basis of the recommendations made by the finance commission of the state'. The 11th Finance Commission found it difficult to work within this frame because of various problems (Refer Chapter-3). For the purpose of avoiding such a situation in future and in order to enable the federal finance commission to take a macro-level view, the provision of Article 280(3) (bb) and (c) maybe amended. The words 'on the basis of

³⁴ Ibid. para-4.14-4.15

the recommendation' in these clause maybe replaced by the words 'after taking into consideration the recommendation'³⁵.

In order to enable the federal finance commission to give due weight to the reports of SFC's for assessing the situation in each state, it is necessary to synchronize the periods covered by the reports of both of them. Since the second generation SFC's has already started working, it will also be creating the same problem for the 12th finance commission. Presently, that part of the provision of clause (1) of article 243-I, which calls for the constitution of SFC at the expiration of every fifth year, created problems to get the objective realized. Hence, in line with Article 280 (1) the words 'or at such earlier time as the Governor considers necessary' maybe added after the words 'fifth year'³⁶.

Taxes on professions, trades, callings and employment under Article 276 have been a source of revenue for the local bodies. One of the impediments in generating substantial revenue from the levy and collection of this tax is that the upper ceiling (presently, Rs.2500 per annum) has been constitutionally fixed (Article 276 (2)). While there is need for fixing the upper ceiling of the tax centrally in order to avoid the charge of double taxation on income, the NCRWC felt that the constitutional provision for this is unnecessary and troublesome. For long, the upper ceiling remained at the unrealistic level of Rs.250 only because of the rather difficult process involved in amending the Constitution. It recommends that it would be better to change this provision and give the necessary legislative power of fixing upper limit to the Parliament. The words 'district board, local boards or any other local authority' as mentioned in clause (1) and (2) of Article 276 maybe suitably replaced by the words 'Panchayats'³⁷.

Now days, the local governments are being encouraged to take recourse to borrowing for financing asset-building and for remunerative

³⁵ Ibid. para-4.22

³⁶ Ibid. para-4.23

³⁷ Ibid. para-4.25

projects. The Panchayats in West Bengal for instance are permitted to borrow from the financial institutions, subject to government approval. With the role envisaged for PRI's in the governance structure, there is no reason why the borrowing power should not be constitutionally given to the Panchayats, especially, the Zilla Parishad. In Chapter 2 of Part 12 of the Constitution, a new Article may be added to allow the Panchayats to borrow from the State government and financial institutions. The Zilla Parishad may, in addition, be permitted to borrow from the capital market³⁸.

Union Ministry of Finance has prepared a set of guidelines for proper utilization of local body grant³⁹:

- (i) Local body grants shall be released to States that have completed the due election process in respect of local bodies. In case of delay in holding local body elections in time, funds will be deducted proportionately.
- (ii) Under the 73rd Amendment, states are expected to devolve responsibilities, powers and resources upon PRI's. Where this has not been done, States should ensure that the same is done no later than 31st March, 2002. The union government shall withhold 25% of the grants meant for PRI's from such states that do not do so as recommended by the respective SFC's upon the local bodies.
- (iii) Details of release of grants to local bodies by the State government in respect of grants received from the Central government on the recommendation of the Tenth Finance Commission and the utilization thereof shall be communicated to the finance ministry.
- (iv) A certificate stating that the grants have been released only to the elected local bodies where elections are mandatory under the Constitution should be furnished to the finance ministry. The first

³⁸ Ibid. para-4.26

³⁹ *Panchayati Raj Upeksha*, ISS, August 2001, p 8

such utilization certificate from the states should reach the finance ministry latest by October, 2002.

- (v) The State governments shall treat expenditure against these grants as part of planned expenditure in their budgets.
- (vi) The local body grant shall not be diverted for any other purpose. Also, the grant shall not be withheld by the State government.
- (vii) No amount from the local body grants should be given to the intermediate or district level Panchayats where these bodies do not have direct responsibilities for maintenance of civic services.
- (viii) These grants will be untied except that they should not be used for payment of salaries and wages.
- (ix) The local bodies shall raise matching resources amounting to not less than 25% of the grant received from the Union Government in case of PRI's. In case any local body is unable to provide the matching contribution; the State government should provide the balance within 3 months, or earlier, to the concerned local body. Grants flowing to local bodies on the recommendations of SFC's or their share in taxes from the states will not be treated as matching contribution.

Summary

It is an absolute truth that no organization can enjoy autonomy without financial self-independence. Thus the freedom and autonomy of local governments in India cannot be maintained by political decentralization without simultaneous economic autonomy with clear-cut devolution of resources by State government. Financial autonomy is sine qua non of the concept of autonomy and self-government of local government in India. The rationale of decentralized governance is derived from the proposition that they are better suited to identifying local problems and resolving them when compared to the centralized

government at the State and the Union levels⁴⁰. Since local problems vary from one sub-region to the other and cannot be brought under a uniform category to be specified for spending money, the Panchayats should enjoy some degree of flexibility for reallocation of resources devolved--- and should enjoy some degree of freedom to spend funds the way they wish to.

The Panchayats should thus enjoy some degree of freedom to spend funds the way they wish. Professor Neela Mukherjee had said, 'in today's world of resource crunch, new and innovative ways of generating and using financial resources from inside is of prime importance of PFI's. For generation and effectively utilizing financial resources, local people's priorities and views should be reflected in planning for such resources and its monitoring'⁴¹. As it is the Amendment is a response to the persistent demand for political, administrative and financial decentralization in a country of continental size with wide regional, linguistic and cultural diversities. The need of the hour is to look into the various recommendations made and thus ensure the success of these institutions. This will strengthen the growing belief that policies, plans and programs for development especially rural development, can only be leavened by direct and active popular participation at the regional and local levels by utilizing the instrumentalities of local self-government.

⁴⁰ Rai, M, et. al. op. cit. p.191

⁴¹Quoted in Mohanty, GR, op. cit. p.152

CHAPTER 5 CONCLUSIONS

The 73rd Amendment Act 1992 maybe regarded as the stepping stone in the evolution of a multi-level federal structure in India. Lord Bryce had said, 'the best school of democracy and the best guarantee for its success is the practice of local self-government'. In a huge federal structure like India with a large population and large regional variations, democracy to be meaningful and welfare-oriented implies decentralization¹. As Mahatma Gandhi had said, 'independence must begin at the bottom. Thus, every village will be a republic or panchayat having full powers. It follows, therefore, that every village has to be self-sustained and capable of managing its affairs. In this structure composed of innumerable villages, there will be ever widening, never ascending circles. Life will not be a pyramid with the apex sustained by the bottom. But it will be an oceanic circle whose centre will be the individual__ __the outermost circumference will not wield power to crush the inner circle but will give strength to all within and derive its own strength from it'².

To ensure people's participation democratic institutions must encourage people's active involvement starting from the lowest practicable level in the body politic. If local and community based approach are strengthened by channelling resources and funds to them and by increasing their control over development initiatives, the society as a whole will benefit and develop.

¹Buch, N, '*Women's Experience in New Panchayats – The Emerging Leadership of Rural Women*' CWDS, Occasional Papers No.-35 ND, 2000, p.1

²Bird, RM, '*Financing Local Services, Patterns, Problem and Possibilities*', in Amanad ed., '*Financing of Panchayati Raj*', Excel Books, New Delhi, 2000, p.65

The 73rd Constitutional Amendment has undoubtedly provided the necessary conditions to bring into existence vibrant local self-governing institutions. It has helped Panchayats in challenging deeply entrenched traditional power structures like those of patriarchy, casteism and feudalism and heralded the way for evolving the Indian polity to a higher plane. Although Panchayats had existed in tradition since ancient times, it is the direct participation and involvement of the local people, which makes it modern and democratic. New social, political and economic areas are constantly being drawn in. In many countries, both developing and developed, hard pressed national governments are increasingly shifting functions to local government in the expectation that additional local resources can be mobilised to pay for them. Moreover regardless of how large or small local governments may be in most countries, they play an important role in the provision and utilisation of local public infrastructure and local public services in general³. This is true in case of India also.

The 73rd Amendment has initiated a process of decentralisation, but decentralisation by itself does not imply democracy. Democracy would truly exist when people at the grass-root level do not merely elect their representatives but are also involved in decision-making, implementation and exercise control and supervision over funds and of their spending. It is generally said that an organisation may be sound but it cannot deliver the goods without adequate financial resources. Finance is thus an essential element which determines the size and magnitude of the activities of an institution and also the degree of decentralised power exercised by it. It is finance which governs its ability to plan and carry out financial responsibilities.

³GoI, '*All India Panchayat Adhyakshas Sammelan*', Ministry of Rural Development, April 2002, p.1

CRISES IN FINANCING OF PANCHAYATS

However, even after a decade since this constitutional amendment was passed, it is universally and acutely realised that the empowerment of the Panchayati Raj Institutions cannot be complete without devolution of adequate and rightful financial and administrative powers to them which unfortunately is far from complete. De-concentration of responsibility has attained momentum, but actual decentralisation in the form of devolution of finances and authorities to Panchayats is still to gain momentum. Hence it is time for all levels of governments in India to change their attitude to the mobilisation and spending of financial resources by the local self-government institutions⁴.

It is obvious that the need has come for a comprehensive view of the working of these grassroot local self-government organisations. If the 73rd Amendment constituted the first generation of Panchayati reforms, there is all round realisation of the necessity to introduce the second generation of Panchayati Raj reforms. What concerns the local self-governing institutions is the need to generate their own resources and reduce their dependence on the Central and State governments.

Earlier an attempt to look into the problems that afflict the working of Panchayats specifically due to paucity of funds has been made. Although PRI does in general have a formidable list of functions to discharge, they do not have the necessary financial resources to cope with these functions. Thus, there is a need to maintain a balance between expanding function and the role entrusted to the local bodies vis a vis their financial resources⁵. It was found that the 73rd Amendment had not made a clear cut financial provision for the lowest tier as the Constitution has made for the centre-state fiscal division. The claim for financial

⁴Ranga Rao, SP, '*State Finance Commission: A Study in Role Perception*', in Konrad Adenauer Foundation, '*National Conference on Emerging Trends in Indian Local Government Finances-October, 1996*', Manohar Publishers, New Delhi, 1998, p.30

⁵ Vithal, CP, and M Sattmathi, '*Panchayati Raj Finance in Andhra Pradesh and Karnataka : an Analysis*', Journal of Rural Development, Volume 15(2), NIRD, Hyderabad, 1996, p.215

betterment has been assured only by the mere provision of the constitution of State Finance Commission (Article 243-I) which cannot create resources but can only make recommendations for distributing of those resources in different proportions⁶. As a result the Panchayats continue to exist at the mercy of the State government for funds. Even after the Amendment was passed the desired attitudinal change amongst the ministers and bureaucracy has not come and the earlier mindset of control and centralisation continues. They see Panchayats as a threat to their own power and influence in rural areas. They fear of not only having to face a powerful local leadership but also that they would be unable to exercise full control over the funds coming to the Panchayats from the central government.

This is also reflected in the passage of State Conformity Acts which in many States are ambiguous regarding the financial provisions related to Panchayats. Also the State governments have not authorised the Panchayats to levy, collect and appropriate such taxes, duties, tolls and fees according to Article 243(H) of the Constitution. As a result the Panchayats greatly rely on the grants they receive from the higher levels of government from time to time. The devolution of funds upon Panchayats is meagre in quantum which hardly leaves any room for the Panchayats to expand the amount as per their priorities.

The Centre and State governments are guilty in creating parallel structures which are para-statal in nature and usurp the lawful areas of functions of Panchayats. The establishment of local area development schemes has been more in keeping with politics than with economics and as a means for ministers to exercise influence in the local area. In the formation and working of State Finance Commissions, unwanted delays, political interference and lack of adequate information and data have

⁶ Mohanty, B and Sabya Sachi Nayar, '*Financial Out Flows Through Local Bodies in Orissa and Prospects of Non-Tax Revenue Generation*', in Mohanty, B, ed., '*Financing the Grassroots Government*', APH Publishing Corporation, New Delhi, 2000, p.185

plagued their smooth functioning. There have been delays in tabling the reports in the State legislature, in accepting recommendations and finally in taking action on the reports presented. The fiscal health of most states in India is itself weak. They are guilty of indulging in populist programs such as subsidising irrigation, electricity and food grains which further jeopardise the chances of Panchayats to gain financial autonomy.

The Panchayats too are guilty of not effectively using their constitutionally guaranteed status to their advantage. There is reluctance to levy taxes at the local level for fear of losing popularity. Lack of information and training prevents many Panchayats to mobilise their own resources to generate funds. Besides apathy, disenchantment with the whole political process and continuance of social differences and status quo have prevented people's mobilisation in many places. These are some of the issues that have adversely affected the working of Panchayats and have been highlighted by various organisations and research groups. It was in this context of growing concern among various sections in the Indian polity that the Government of India organised the All India Panchayat Adhyakshas Sammelan which was held in New Delhi on 5th & 6th April, 2002 to build a consensus on the measures needed to revitalise the Panchayati Raj system.

ALL INDIA PANCHAYAT ADHYAKSHAS SAMMELAN

At the All India Panchayat Adhyakshas Sammelan a 'National Declaration' was adopted which included among other recommendations, the following with regards to financing of Panchayati Raj Institutions⁷:-

- All State governments shall take action to devolve funds, functions and functionaries to the Panchayati Raj institutions before 31st December 2002. In doing so they will be guided by the

⁷ GoI, '*All India Panchayat Adhyakshas Sammelan*', Ministry of Rural Development, April 2002, Pp.1-4

recommendations of the Task Force on Devolution of Powers and Functions upon Panchayati Raj institutions set up by the Ministry of Rural Development, Department of Panchayati Raj.

- There is a major mismatch between the responsibilities and the resources of Panchayati Raj institutions. The State governments will do everything required to ensure by 31st December, 2002 that Panchayati Raj institutions have the requisite financial resources and powers. In particular, they will, implement the recommendations of the state finance commissions to enable the Panchayati Raj Institutions to raise the requisite resources.

- In addition, the Union government is urged to devise an appropriate mechanism to provide significant non-budgetary resources in the form of loans with adequate maturities to Panchayati Raj Institutions, specifically to be used for such developmental projects as are planned and executed by Panchayati Raj Institutions themselves.

- State governments will take action, before 31st December, 2002, to ensure that parallel bodies, if any, particularly at the village level function under the guidance of the Panchayats.

- The Panchayats need to be given adequate control over natural resources-land, water, minor forest produce and minerals. The State governments will make suitable provisions or amendments, before 31st December 2002, in the laws and rules governing these subjects.

- An appropriate structure of incentives will be put in place by the State and the Central governments to recognise and encourage the Panchayats for outstanding performance.

At the end of the Sammelan, the PM of India proposed the need for an appropriate new amendment to the Constitution to bring about speedy and effective devolution of financial and administrative powers to Panchayati Raj Institution. The need thus arises for all political parties and Members of Parliament to pass the amendment and usher in the era of second generation of Panchayati reforms which is what the National

Commission to Review the Working of the Constitution (2000) has recommended in its paper on Panchayati Raj institutions.

The Indian Prime Minister Shri Atal Behari Vajpayee had said, 'let us strengthen the institutions and systems that promote transparency and effective public participation at every level. That can only come through a movement. Most of the states have taken steps towards decentralisation in terms of elections and devolution of resources. I would like the others to complete the process at the earliest'⁸.

The Minister of Rural Development Shri M. Venkaiah Naidu said, 'I believe that democracy, devolution and development are the three pillars to any poverty alleviation approach. Therefore, effective functioning of Panchayati Raj Institution is a National Commitment'⁹.

Finance Minister Yashwant Sinha suggested that local area development funds sanctioned to MPs and MLA's should be spent through Panchayats. Panchayat heads had expressed their anguish at being sidelined by the officialdom and made demands, besides other things, for an increase in funds¹⁰. Such views reveal the growing consensus amongst the various political leaders for necessary steps to be undertaken to overcome these problems.

MEASURES TO IMPROVE PANCHAYATS FINANCES

As has been emphasised time and again, the financial autonomy is the sine qua non of the concept of autonomy and democracy of local self-government in India. It is not the 'untied funds' of the State and Central governments which will guarantee the financial autonomy rather the innovative resource mobilisation by Panchayats for generation of income from entrepreneurial activities, project tied loans etc. Fiscal autonomy

⁸ Ibid. p.2

⁹ Ibid. p.3

¹⁰ *Panchayati Raj Update*, ISS, April 2002, p.5

cannot be built on a regime of grants and aids. The PRI's can play a genuine role in local development and self rule only if they enjoy some degree of fiscal autonomy. This attribute is clearly more than relying on untied funds and rests on the innovative resource mobilisation, including project tied loans, public contributions and the like. Tax assignments with clear taxing powers and tax sharing, assumes significance in this context. A few other aspects that are important in inter-governmental fiscal transfers are the timing, frequency and the amount that must be known in advance to enable the receiving unit to do proper budgeting and planning. They should not be left to executive decisions but should be made transparent through the budget documents¹¹.

Why to Mobilise 'Own Resources'?

The need to mobilise own resources assumes significance due to the number of advantages it provides the Panchayats¹² -

- a) The imperative need to augment the natural resources of the Panchayats is because the absence of/meagre mobilisation of local resources will not permit the Panchayats to provide at least the minimum basic services to their people.
- b) It would also enable them to make any matching contribution for the finance commission grants or other matching grants of state governments.
- c) In utilising the resources mobilised through their own effort, Panchayats will be more careful in choosing the items on which funds will be spent. Greater dependence on government grants will increase government control over them and reduce their functional autonomy as well as decision making powers.

¹¹Oommen, TK, '*Panchayat Finances and Issues Relating to Intergovernmental Transfers*', in Oommen, TK, and Datta, A, '*Panchayats and their Finances*', Concept, New Delhi, 1995, p.25

¹²NIRD, '*All India Panchayat Adhyakshas Sammelan: Theme papers*', Hyderabad, 2002, p.21

d) People's involvement, participation and awareness regarding local governance, Panchayati activities and development projects will be greater if they pay taxes and non-taxes to the Panchayats.

e) Panchayats may not be able to appoint any staff or achieve the goal of becoming institutions of self-governance if they do not have own resources mobilised from their localities. Such exercises will also cover the provisions of the Constitution amendment which endowed the Panchayati Raj bodies with greater responsibility than ever before.

How to Increase Resources?

The question thus arises as to how Panchayats can mobilise and increase their resources. It is imperative that to generate their own resources, Panchayats should be authorised to collect taxes such as tax on lands and buildings, profession tax, entertainment tax, tax on agricultural holdings etc. Tax on land and building must be made an obligatory tax in the sense that its levy must be made compulsory for the Panchayati Raj Institutions. As a result they will earn significant revenue if they fix the rates at a reasonable level, revise their assessment at least once in every 5 years and collect the tax fully each year. In addition to this tax, Panchayats should also make sincere efforts to levy other taxes transferred to them under their State Panchayati Acts. This tax is very productive if levied regularly according to the procedures and rules prescribed by the State governments¹³.

Panchayats should besides mobilising local resources also tap local human resources by engaging people directly in the developmental activities. In the long run, Panchayats can improve their own resources only through non-tax resources and may not depend only so much on State or Central government grants. Besides the Central and State government should make attempts to do away with parallel structures wherever they exist and give greater responsibility to Panchayats, provide

¹³ Ibid.

training and information in finance and account management, ensure that all developmental activities particularly anti-poverty programmes are carried out through the Panchayats and that they have the autonomy to manage the finances as they would acquire greater coherence and State governments need to ensure that timely action is taken with regards to appointment of the State Finance Commission and appropriate measures taken on the report submitted. What is needed, besides political will on the part of the State government to devolve financial powers to Panchayats and ensure their autonomy, is for the Panchayats to mobilise their own resources and embark on a self-help attitude.

To improve the overall efficiency in governance it is necessary that certain issues be looked into which are closely linked to the proper working of Panchayats. The conceptual issues that are common for all and relate to the nature of the Panchayats are-

- a) Conceptualising Panchayats as institutions of self-government in the local areas and not as arms of the State government to implement some of its schemes.
- b) Envisaging preparation of plans for economic development and social justice in respect of the local area and implementing them as the primary tasks.
- c) Establishing the need for vertical linkages between different tiers of PRI, as each tier forms part of the edifice of Panchayati Raj as well as between the central, state and local governments¹⁴.

Thus the Panchayati Raj system needs to be revamped with the following objective-

- ensuring people's participation in local level administration,
- designing innovative methods for enhancing the level's of peoples involvement and inculcating a sense of responsibility with regards to developmental activities in the village,

¹⁴ GoI, '*All India Panchayat*', op. cit. p. 28

- ensuring the benefit of developmental schemes reaches those whom they are intended for¹⁵.

ISSUES FOR THE FUTURE

While finance is perhaps the most important dimension in the smooth working of Panchayats, there are also other related issues which also need to be looked into. Thus some of the issues that call for immediate attention of the central, state and local governments to enable PRI's to function as institutions of self-government and attain financial reliance are as follows¹⁶-

- What role can the Central and State governments play in facilitating the process of devolution of functions, funds and functionaries in accordance with the spirit of the constitution?
- Need to increase the level of awareness of powers granted to different levels of Panchayats in each State for the mobilisation of own resources through tax and non-tax resources,
- Improving the capacity and willingness of the Panchayats to levy taxes, increase their tax and non-tax rates ensuring their prompt and full collection,
- Identify the present difficulties in the area of mobilisation of their own revenue by Panchayats and suggestions to overcome them,
- What are the additional powers required by the Panchayats to increase the size of their own revenue?
- The transfer of the minimum financial autonomy needed as a pre-requisite for Panchayats to become institutions of self-government.
- To reiterate, the recommendations of the State Finance Commission must lay the foundation of a decentralised but sound

¹⁵ Ibid. p.1

¹⁶ Ibid. Pp.19-23

public finance in the Indian federal system, besides promoting regional balance especially through ensuring certain basic services of reasonable quality. The scheme of fiscal devolution flowing from the SFC recommendations will have to promote not only financial autonomy but functional and administrative autonomy as well. But besides fulfilling the Constitutional demand, the Panchayats must also be able to raise their own resources to gain financial independence.

TOWARDS A MULTI-FEDERAL DEMOCRACY

The Sarkaria Commission Report (1988) in its concluding chapter drew attention to the importance of a decentralised polity in the following terms- "Decentralisation of real power to these local institutions would thus help diffuse the threat of centrifugal forces, increase popular involvement all along the line, broaden the base of our democratic polity, promote administrative efficiency and improve the health and stability of inter-governmental relations"¹⁷.

India began to face fundamental changes in various fields in the past decade. The pace of socio-economic change in India has accelerated considerably by giving rise to new strains and testing the capacity of the federal system to organise and promote incremental reform. The inadequacies of crises arrangements have become all too apparent and the need for a more flexible and finely calibrated system of responses has assumed urgency. It was felt that the empowerment of local communities as distinct components of the federal system will require much ingenuity, particularly since most of the models available were worked out in less

¹⁷ Mukarji, N and B. Arora, 'Conclusion: Restructuring Federal Democracy', in Mukarji, N, and Arora, B, ed., 'Federalism in India', Vikas, New Delhi, 1992, p.274

populace polities¹⁸. A third stratum of self-government was the structural invention needed. It has thus become clear that in India, restricting the federal principle to two levels would impoverish it. Downward extension of the federal principle would ultimately strengthen democratisation at all levels. It meant moving to a multi-level arrangement whereby, "India would then have a cascading federalism, a 'federation of federations'". Each state would become a federation of self-governing districts similarly a federal grouping of sub-district institutions of self-governance¹⁹.

Since early 1990s when India had embarked on the process of liberalisation, the concern for the country being integrated in the process of globalisation as well as ensuring the welfare and development of the populace at large has been a major concern. Since global forces go beyond territorial boundaries and affect people variedly in different parts of the globe, in a vast country like India with over one billion people and regional, linguistic and cultural differences, the citizen's increasing participation in decision making on issues that affect their lives- fighting poverty, developing human resources and social welfare- becomes imperative. The 73rd Amendment was such a revolutionary step in this direction bringing the power structure closer to the people and enlarging the scope of democracy.

The status of PRI's varies greatly from state to state in terms of devolution of powers and functions to these institutions, socio-economic profile of villages, educational and cultural attributes of the elected representatives etc. There is thus need to provide a sustained professional back-up, so that they have the up-to-date knowledge on the dynamics of development programs. Keeping in view the federal character of the Indian union there should not be any rigidity in the pattern to be

¹⁸Arora, B, 'Adapting Federalism to India: Multi-level and Asymmetrical Innovation,' in Arora,B and D. Verney, 'Multiple Identities in a Single State Indian Federalism in Comparative Perspective,' Konark, New Delhi, 1995, p.94

¹⁹ Ibid. p.270

adopted for different States and regions of the country. What is most important is that underlying the diversities of pattern there should be genuine transfer of power to the people. It is probably this idea that has shaped Article 243G of the Constitution, which provides for discretion in a manner that facilitates transformation of the PRI's into wholesome, autonomous institutions of self-government. The principle of decentralisation should inform all layers of governance and the process of its implementation must be approached in a holistic manner.

But as has been seen the financial devolution has been more to satisfy the letter of law than keeping to the spirit of self-government.

However we have to travel far beyond fiscal federalism in moving towards the goal of building institutions of self-government. This can be achieved only if the transitional task is pursued with clarity of purpose and dedication to the cause of democratic decentralisation and finance is made to play the inimitable mid-wifely role in this task²⁰. That is, a recognition of finance as a means for the ultimate benefit of the people and not as a means to wield unwanted control over the local bodies. Ultimately just as India is a 'union of states', states should be union of district and district unions of sub-state level. Panchayat finance is necessary, though not a sufficient one towards realising this task.

Economic efficiency and equity which are basic considerations in fiscal transfers must be kept fully in view in regard to sub-state level fiscal transfer as well as clearly, some degree of inter-panchayat equity has to be insured. This pre-supposes some measure of inter-state equity to which the Union Finance Commission has to address. Net fiscal benefits as far as possible should be equal across localities. Over a period of time, the goal of fiscal transfers should help facilitate this on a planned priority basis so that each gram panchayat has comparable levels of fiscal burden

²⁰ Datta, A. 'Finance Commissions and Restructuring of Panchayat Finances', in Oommen, TK, and Datta, A, 'Panchayats and their Finances', Concept, New Delhi, 1995, Pp.32-33

(taxation). This is the best way to ensure horizontal equality²¹. Tax coordination to ensure some measure of interstate equity and inter-district rationalisation in the rates of commodities is needed particularly in view of the possibilities of competitive taxing, tax rating, tax concessions etc. to attract investment from potential firms and entrepreneurs by the states and PRI's are more relevant now than ever before.

FUTURE OF FEDERALISM IN INDIA

We are at the commencement of a process in which the bureaucracy has to yield space to representatives of the people. Any attempt to stream-roller the States which represent linguistic-cultural groups of nationalities with their own distinct features would weaken rather than strengthen the Centre. The role of local government institutions, cooperative organisations, regional development boards and voluntary agencies is also an important element in any vibrant federal polity²².

Following the theoretical and empirical literature on federalism, decentralisation and fiscal devolution, certain principals in designing inter-governmental fiscal transfers are outlined below²³-

- Transparency- the basis on which transfer's is made must be clearly stated.
- Predictability- Inter-governmental transfer's mechanism should ensure predictability of sustainable government shares from year to year to permit advanced planning.

²¹Oommen, TK, op. cit. p.25

²²Chaturvedi, TN and A Datta, 'Introduction', in Chaturvedi, TN and A Datta, ed., 'Union State Relations', IIPA, New Delhi, 1984, p-iv

²³ISS, 'Devolution of Resources to Rural Local Bodies, a Comparative Study of Select State Finance Commission Reports', ISS, New Delhi, 2001, Pp.10-11

- **Autonomy-** sub-national governments should have complete independence and flexibility in setting their own development priorities.

The outcomes of a decentralisation policy will depend not just on the 'relative weights of devolution and de-concentration in the institutional and fiscal structures'²⁴, but also on their combination with other important elements such as holding of timely election, participation of women, backward classes, scheduled castes and scheduled tribes in large numbers, political will and mobilisation of the people. A country (like India) born out of a classic liberation struggle must show the vision and courage to reorder its priorities, reformulate its basic assumptions, rearrange its political structures and reconstruct its federal edifice in consonance with new demands and requirements of its people and the polity²⁵.

This ability was reflected in the 73rd Amendment Act 1992, which finally guaranteed constitutional status to Panchayati Raj institutions in India. Federal democracy can survive and flourish in India only to the extent it can accommodate the rising tide of pressure for peoples participation in the political and development process. There is a need for intermediate structures of governance which effectively shorten the distance between the people and the apparatus, thereby making it possible for participative upsurges to be absorbed. Creative decentralisation as a policy is thus an essential prerequisite for further thinking on Indian federalism. Multi-level federalism needs to be seen as the structural means through which self-governing units in such a scheme will need to draw sustenance from grass roots movement. Such a radically new approach might help to meet the challenge, of pressures from below for effective political participation²⁶.

Conclusions that emerge from the above analysis are-

²⁴ Crook, R C and J Manor, '*Democracy and Decentralisation in South Asia and West Africa*', Cambridge University Press, Cambridge, 1998, p.2

²⁵ Khan, R, '*Federal India a Design for Change*', Vikas, New Delhi, 1992, p.89

²⁶ Mukarji, N and Arora, B, '*Conclusion*', op.cit. p.270

- The Panchayats are to be strengthened as institutions of self-government and not merely as agents of state plan implementation.
- The fiscal strengthening of the Panchayats involves simultaneous measures for fiscal and organisational contraction of the State government.
- The state field staff transfer strategy to the Panchayats prevents fiscal decentralisation to take root.
- Fiscal accountability of the Panchayats is to be controlled and related to their constituents²⁷.

Democratic decentralisation offers better coordination as it offers a combination of integrated administration and coordination from below, namely, the representatives of the clients of administration, who in democracies are the people. It combines the political and economic factors and offers the necessary heterogeneity. It avoids exclusiveness. It has the potential of realising Gandhiji's dream of a casteless society²⁸.

It is universally recognised that major rethinking lies ahead on the adaptation of existing structure to the rapidly changing needs of the times. Slowly but surely, local democracy is emerging as the controlling factor. The process is uneven in the different states, but the process is on and holds much promise for the future. Multi-level federalism appears to offer the greatest scope and possibilities for meeting the indispensable coherence requirement of a strong and united Indian state²⁹. By making Panchayats administratively and financially autonomous, the federal, democratic setup in India as well as development process and social welfare will be strengthened.

²⁷ Datta, A, op.cit p.33

²⁸ *Panchayati Raj Update*, ISS, May 2002, p.8

²⁹ Mukarji, N and Arora, B, 'Conclusion', op.cit. p.273

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WEBSITE

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ANNEXURE-1

SCHEDULE-XI

- 1 Agriculture, including agricultural extension.**
- 2 Land improvement, implementation of land reforms, land consolidation and soil conservation.**
- 3 Minor irrigation, water management and watershed development.**
- 4 Animal husbandry, dairying and poultry.**
- 5 Fisheries.**
- 6 Social forestry and farm forestry.**
- 7 Minor forest produce.**
- 8 Small scale industries, including food-producing industries.**
- 9 Khadi, village and cottage industries.**
- 10 Rural housing.**
- 11 Drinking water.**
- 12 Fuel and fodder.**
- 13 Roads, culverts, bridges, ferries, waterways and other means of communication.**
- 14 Rural electrification, including distribution of electricity.**
- 15 Non-conventional energy sources.**
- 16 Poverty alleviation programme.**
- 17 Education, including primary and secondary schools.**
- 18 Technical training and vocational education.**
- 19 Adult and non-formal education.**
- 20 Libraries.**
- 21 Cultural activities.**
- 22 Markets and fairs.**
- 23 Health and sanitation, including hospitals, primary health centers and dispensaries.**
- 24 Family welfare.**
- 25 Women and child development.**
- 26 Social welfare, including welfare of the handicapped and mentally retarded.**
- 27 Welfare of the weaker sections, and in particular, of the Scheduled Castes and Scheduled Tribes.**
- 28 Public distribution system.**
- 29 Maintenance of community assets.**

Source: Government of India, 'Report of the Task Force on Devolution of Powers and Functions upon PRI's', 2001, p.52